

PREM 19/1584

PART 7

MT

SECRET

CONFIDENTIAL FILING

SHP BUILDING POLICY  
SHP BUILDING PAY

NATIONALISED

INDUSTRIES

PART 1 MAY 1979

PART 7 JUNE 1984

Referred to	Date	Referred to	Date	Referred to	Date	Referred to	Date
<del>June 1984</del>		5.9.84					
<del>20.6.84</del>		13.9.84					
<del>21/6/84</del>		17.9.84					
<del>22/6/84</del>		20.9.84					
<del>24/7/84</del>		15.10.84					
<del>5.7.84</del>		16.11.84					
<del>6.7.84</del>		27.11.84					
<del>11.7.84</del>		5.12.84					
<del>11/7/84</del>		21.12.84					
<del>11/7/84</del>		23.12.84					
<del>16.7.84</del>		23.1.85					
<del>17.7.84</del>		24.1.85					
<del>19.7.84</del>		25.1.85					
<del>24/7/84</del>		28.1.85					
<del>25.7.84</del>		29.1.85					
<del>27.7.84</del>		31.1.85					
<del>28.8.84</del>							
<del>9.8.84</del>							
<del>28.8.84</del>							

PREM 19/1584

Material used by  
official Historian  
Part 6 and  
DO NOT DESTROY

PART 7 ends:-

CST to MS (DTI) 31.1.85

PART 8 begins:-

DTI to MOD 4.2.85

TO BE RETAINED AS TOP ENCLOSURE

### Cabinet / Cabinet Committee Documents

Reference	Date
E(A)(84) 32	06.06.84
E(A)(84) 15 <sup>th</sup> Meeting, Minutes	20.06.84
E(A)(84) 43	13.07.84
C(84) 19	16.07.84
E(A)(84) 19 <sup>th</sup> Meeting, Minute 1	18.07.84
CC(84) 27 <sup>th</sup> Conclusions, Minutes 1 and 5	19.07.84
E(NI)(84) 11	12.09.84
C(85) 3	22.01.85
CC(85) 3 <sup>rd</sup> Conclusions, Minute 6	24.01.85
CC(85) 4 <sup>th</sup> Conclusions, Minute 2	31.01.85

The documents listed above, which were enclosed on this file, have been removed and destroyed. Such documents are the responsibility of the Cabinet Office. When released they are available in the appropriate **CAB (CABINET OFFICE) CLASSES**

Signed Wayland Date 11 March 2014

**PREM Records Team**

## Published Papers

The following published paper(s) enclosed on this file have been removed and destroyed. Copies may be found elsewhere in The National Archives.

1. House of Commons Hansard, 27 June 1984,  
Columns 1093-1113 "British Shipbuilders"
2. House of Commons Hansard, 27 November 1984,  
Columns 832-878 "Shipbuilding Industry"
3. House of Commons Hansard, 28 January 1985,  
Columns 21-27 "Frigate (Orders)"

Signed Wayland Date 11 March 2014

**PREM Records Team**

CONFIDENTIAL



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CNP

1/2.

Treasury Chambers, Parliament Street, SW1P 3AG

Norman Lamont MP  
 Minister of State for Industry  
 Department of Trade and Industry  
 1 - 19 Victoria Street  
 London  
 SW1H 0ET

31 January 1985

Dear Minister

BRITISH SHIPBUILDERS - ORDER PROSPECTS,  
FLEXIBILITY AND CONTROL

I am sorry not to have been able to reply before now to your letter of 21 December, but I wanted to take stock of the position we have reached on shipbuilding policy as a whole.

The present state of affairs is far from satisfactory. We are supporting in public ownership, at considerable expense, a merchant shipbuilding industry which we are advised has no prospect of commercial viability. This leads us not only to argue in Brussels - contrary to our general policy of supporting international arrangements to reduce and phase out subsidies - for approval of increased overt support for British Shipbuilders, but also to use various covert subsidies. Indeed the request in your letter for my agreement to include soft credit for export orders in the new financial control system would institutionalise a covert subsidy of a kind we have hitherto hesitated to use.

When we agreed collectively last June to limit new orders taken by BS merchant shipbuilding yards to 100,000 cgrt by 1986-87 we regarded that as the toughest option next to immediate closure of the yards. It was necessary to take that severe line in order to end as rapidly as possible the unsatisfactory position I have just described. I therefore welcomed the new financial control system as a means of enforcing our collective decision, but the new control regime will be effective only if the annual limits are set very tightly. We have now set limits for the first two years which you say are the maximum compatible with last year's decision. No doubt you will soon need to set a limit for 1986-87 itself. I would hope that this could be somewhat less than the maximum in order to give some room for manoeuvre.

CONFIDENTIAL

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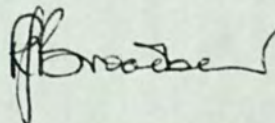
Having set this new system in place I hope, in the spirit of recent report by the Financial Management Unit, that in monitoring progress we can collect the information necessary to judge how effective the policy is in improving the cost-effectiveness of subsidy and the level and intensity of subsidy per ship.

I note how you are proposing to handle negotiations in Brussels. Whilst I do not object to this, I remain uneasy about the apparent necessity to increase subsidies to BS, which reinforces my wish to ensure that we stick to the plan we agreed last June.

Finally, as to special credit for export orders, I acknowledge that their inclusion in the financial control system marginally strengthens our, rather weak, defences if we are found out in this breach of our obligations. Since I understand that we are certainly not alone in breaching them, I am reluctantly willing to agree to your proposed method of handling them.

I am copying this letter to the Prime Minister, Sir Geoffrey Howe, Douglas Hurd, to members of E(A) and to Sir Robert Armstrong.

*Yours sincerely*



PETER REES

*[Approved by the Chief Secretary]*

CONFIDENTIAL

Nat Ind: Shipbuilding Pt 7.

ET FEB 1985

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File

Prime Minister ②  
To note

AF 30/1

SCOTTISH OFFICE  
WHITEHALL, LONDON SW1A 2AU

CONFIDENTIAL AND CMO

Sir Robert Armstrong GCB CVO  
Cabinet Office  
Whitehall  
London  
SW1A 2AS

30 January 1985

*mt*

Dear Robert,

FRIGATE ORDERS

As you know, I raised no objection to the arrangements for allocating frigate orders proposed in the note attached to your minute of 25 January because I support the general aim of rewarding moderation.

Nevertheless I am concerned about the high direct and indirect costs of these arrangements, and about their likely effect on the Government's privatisation programme and on Yarrow Shipbuilders. In particular the bringing forward of a Type 23 frigate and its allocation to Swan Hunter on a non-competitive basis will be seen as a blow to the hopes of Yarrow that they would be able to establish, on their merits, a strong position in relation to the Type 23, in overseas as well as home markets.

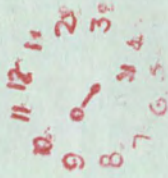
I am sending copies of this letter to the Prime Minister and other members of the Cabinet.

*Yours ever,*

*George*

\_\_\_\_\_

30 JAN 1965



NAT (WD)  
Supplies  
Part 7



Ref. A085/315

PRIME MINISTER

Orders for Frigates

The Cabinet minutes of last Thursday's discussion of Type 22 frigates (CC(85) 3rd Conclusions, Minute 6), as circulated, merely say that the Cabinet agreed to resume their discussion of this matter at the earliest opportunity. We shall need to record in this week's minutes:

FLAS A

- (i) that a solution to the problem of finding sufficient work for Cammell Laird without unreasonable detriment to Swan Hunter, and to the overall financial position of British Shipbuilders (BS), was subsequently devised by the Ministers most closely concerned;
- (ii) that the proposal was, on your instructions, circulated to members of the Cabinet under cover of a minute to the Lord Chancellor from the Secretary of the Cabinet dated 25 January.
- (iii) that the Cabinet approved the proposal subject to a qualification by the Chancellor of the Exchequer (his Private Secretary's letter of 28 January) that the extent of any further increase to the External Financing Limit of BS which might be necessary to take account of adverse effects on the Yarrow privatisation should be considered later when the outcome of the sale was known;
- (iv) that the Secretary of State for Defence made an announcement about the orders for frigates in an oral statement in the House of Commons on 28 January.

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C.L. - P...  
75 - KPL  
15-12-85  
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23



2. You will wish to make a brief oral report on these developments, so that the story can be properly rounded off in the Cabinet minutes.

RA

ROBERT ARMSTRONG

29 January 1985

CONQUEROR



NDPM

AAD

SCOTTISH OFFICE  
WHITEHALL, LONDON SW1A 2AU

COMMERICAL - IN CONFIDENCE

The Rt Hon Norman Tebbit MP  
Secretary of State for Trade and Industry  
Department of Trade and Industry  
1-19 Victoria Street  
LONDON  
SW1H 0ET

29 January 1985

*Dear Norman,*

WARSHIP BUILDING PRIVATISATION: TRAFALGAR HOUSE INTEREST

I have seen your letter of 23 January to Michael Heseltine about the privatisation of Yarrow Shipbuilders Ltd (YSL) and Vickers Shipbuilding and Engineering Ltd (VSEL).

I can see that if TH want to pursue their bid for YSL they must be allowed to do so, but I am concerned about the possibility of a further concentration of market shares, for both warshipbuilding and the offshore industry, in the hands of Trafalgar House: I have no doubt that they would be ruthless in their exploitation of any commercial advantage that they might gain if they were to obtain a dominant position in any one sector.

The benefits of privatisation must be judged not only in relation to the cash proceeds at the time of sale but also, and in my view more importantly, in relation to the benefits to the economy from improvements in efficiency and competition in the future. I do not see that we help the latter if we adopt a sales policy which tends to substitute a strong private monopoly for a weak public monopoly which never behaved as such.

I would like therefore to see a strengthening of the warning about competition which you suggest in paragraph 2 of your letter; in particular I would prefer to see omitted the qualification about "a close contest for VSEL", so that the last sentence would be on these lines: "In deciding whether to give its consent to a particular sale the Government will take account of all relevant factors, including particularly its aim to bring about a competitive market in warship building". It would then be for Trafalgar House to decide

in the light of this how they want to play their hand.

I am sending copies of this letter to the Prime Minister, Michael Heseltine, to the other members of E(A) and to Sir Robert Armstrong.

Yours truly,

George

Shipbuilding.

29 JAN 1985



*See my CP*



MINISTRY OF DEFENCE  
MAIN BUILDING WHITEHALL LONDON SW1  
Telephone 01-~~8307822~~ 218 2111/3

MO 26/3/1

28th January 1985

*Dear Charles,*

ORDERS FOR FRIGATES

Subject to the agreement of his Cabinet colleagues to the proposals set out in the attachment to Sir Robert Armstrong's minute of 25th January to the Lord Chancellor, my Secretary of State proposes to announce the decisions by means of an oral statement to the House this afternoon. You told me on Friday that the Lord Privy Seal would have no objection to this course of action. I attach a copy of the first draft of Mr Heseltine's statement.

2. I am sending copies of this letter and the attachment to Charles Powell (Prime Minister's Office), Janet Lewis-Jones (Lord President's Office), David Peretz (Treasury), Callum McCarthy (Department of Trade and Industry), Murdo MacLean (Chief Whip's Office) and Richard Hatfield (Cabinet Office).

*Yours ever,*

*Dennis Brennan*

(D BRENNAN)  
Private Secretary

C Marshall Esq  
Lord Privy Seal's Office



## COMMERCIAL IN CONFIDENCE

DRAFT STATEMENTFRIGATE ORDERS

As the House knows, I have been considering the results of a tendering exercise for two Type 22 frigates for the Royal Navy. Cammell Laird, Swan Hunter and Vosper Thornycroft were each invited to tender for these warships, one the fourth replacement for warships lost in the South Atlantic and the other an addition to the naval programme which I authorised in 1983.

The tendering process has been unusually protracted for several reasons. I have been concerned to obtain the best available prices and tauter contract terms than we have been accustomed to in this field of defence procurement. The earlier tender replies did not adequately contribute to this objective, and it was not possible to take a decision on the order before the validity of the tenders expired. A final round of tendering was initiated in late July last year. The results of this round met several of the concerns to which I have referred; and, as with the earlier rounds, showed that the competition had been keenly fought and close.

The House will be aware that the decision on the orders for these frigates has important implications for each of the competing yards. I have considered these implications carefully, in consultation with my Ministerial colleagues.

COMMERCIAL IN CONFIDENCE

CONFIDENTIAL

## COMMERCIAL IN CONFIDENCE

At this point, I would like to make it clear that the deplorable and unnecessary industrial action which occurred last summer at Cammell Laird would, had it continued, have excluded the yard from further consideration in the competition. The courage and determination shown by the moderate elements of the workforce at Cammell Laird, in the face of the intimidatory behaviour of their former work colleagues, has averted the almost certain closure of the yard at an early date.

In the light of this and other relevant factors, I have decided that an order for one Type 22 frigate will be placed with Cammell Laird and for the second with Swan Hunter. This will ensure the <sup>the prospect is</sup> survival of Cammell Laird <sup>will continue</sup> as a major warship-builder, and I hope that the yard will succeed in obtaining other business in the short as well as the long term.

Swan Hunter, which is a much larger firm and is implementing a large redundancy programme at the moment, faces further substantial redundancies even with the order which I have just announced. Last autumn, we embarked on the construction of a new class of frigates, the Type 23, and placed a first order at Yarrow on the Clyde. I have decided to place an order for the second Type 23 frigate at Swan Hunter as soon as this can sensibly be done, and subject to satisfactory agreement on price and other contract terms. I will expect the price for this frigate to reflect the economies obtainable with an order for two frigates rather than one;

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COMMERCIAL IN CONFIDENCE

and to be competitive. With the latter purpose in mind, tenders will be invited in the same timescale from all United Kingdom yards capable of carrying out the work for a further Type 23 frigate order [for one and possibly more ships.]

These decisions mean that new work at Vosper Thornycroft will have to await the outcome of other current tendering exercises. That yard has recently submitted tenders which are under consideration for 2 MCMVs; I am awaiting a tender from them for the first-of-class of the new Single Role Mine-hunter; and I wish them every success in their current efforts to obtain major export work.

COMMERCIAL IN CONFIDENCE

CONFIDENTIAL

File

STATEMENT

FRIGATE ORDERS

As the House knows, I have been considering the results of a tendering exercise for two Type 22 frigates for the Royal Navy. Cammell Laird, Swan Hunter and Vosper Thornycroft were each invited to tender for these warships, one the fourth replacement for warships lost in the South Atlantic and the other an addition to the naval programme which I authorised in 1983.

The tendering process has been unusually protracted for several reasons. I have been concerned to obtain the best available prices and tauter contract terms than we have been accustomed to in this field of defence procurement. The earlier tender replies did not adequately contribute to this objective, and it was not possible to take a decision on the order before the validity of the tenders expired. A final round of tendering was initiated in late July last year. The results of this round met several of the concerns to which I have referred; and, as with the earlier rounds, showed that the competition had been close and keenly fought.

The House will be aware that the decision on the orders for these frigates has important implications for each of the competing yards. I have considered these implications carefully, in consultation with my Ministerial colleagues.

At this point, I should say that the deplorable and unnecessary industrial action which occurred last summer at Cammell Laird would, as I made clear at the time, had it continued, have excluded the yard from further consideration in the competition. The courage and determination shown by the moderate elements of the workforce at Cammell Laird, in the face of the intimidatory behaviour of their former work colleagues, has averted the almost certain closure of the yard at an early date.

The cheapest solution from the point of Defence procurement would be to place the order for both ships with one yard but in the light of the wider and relevant factors involved, I have decided that an order for one Type 22 frigate will be placed with Cammell Laird and for the second with Swan Hunter, and I am prepared to authorise the necessary expenditure. This offers the prospect of survival of Cammell Laird as a major warshipbuilder; without such a contract the yard would have closed. I hope that the yard will succeed in obtaining other business in the short as well as the long term.

Swan Hunter, which is a much larger firm and is implementing a large redundancy programme at the moment, faces further substantial redundancies even with the order which I have just announced. The Government wish to do what they reasonably can to prevent this. Last autumn, we embarked on the construction of a new class of frigates, the Type 23, and negotiated a first order at Yarrow on the Clyde. I have decided to negotiate an order for the second Type 23 frigate at Swan Hunter as soon as this can sensibly be done, and subject to

satisfactory agreement on price and other contract terms. I will expect the price for this frigate to reflect the economies obtainable with an order for two frigates rather than one; and to be competitive. In order to establish this, tenders will be invited for the third Type 23 order in the same timescale from all United Kingdom yards capable of carrying out the work.



Treasury Chambers, Parliament Street, SW1P 3AG  
01-233 3000

28 January 1985

Richard Hatfield Esq  
Private Secretary to  
Sir Robert Armstrong  
Cabinet Office

*Dear Richard*

**ORDERS FOR FRIGATES**

The Chancellor has seen Sir Robert Armstrong's minute of today. He agrees to the proposals, with one important qualification. Any reduction in receipts from the sale of Yarrow (paragraph 5 of the attachment) will be difficult to quantify, as the note recognises. The Chancellor believes that the proposed increase in the British Shipbuilders' EFL on this account should be considered later, when the outcome of the sale is known.

Copies of this letter go to Andrew Turnbull (No.10), Richard Mottram (MOD) and Callum McCarthy (DTI).

*Yours ever  
Rachel.*

MRS R LOMAX  
Principal Private Secretary



10 DOWNING STREET

*From the Principal Private Secretary*

SIR ROBERT ARMSTRONG

ORDERS FOR FRIGATES

The Prime Minister was grateful for your minute of 24 January (A085/258) attaching a note on the proposal for resolving the problem discussed at Cabinet yesterday.

You told the Prime Minister that you had received three comments on this from Departments:-

- (i) The Ministry of Defence had suggested an amendment to paragraph 2(4) indicating that not only the amount required to keep open the option to privatise Cammell Laird but also its distribution between the programmes of the Secretaries of State for Defence and Trade and Industry was a matter for future discussion. The Prime Minister was quite clear that she had agreed with the Secretary of State for Defence that his programme would bear the whole of such a sum; and that this amendment should be rejected.
- (ii) It had also been suggested that a sentence should be added to paragraph 2(4) to make clear that there might be additional costs from letting the Type 23/02 contract to Swan Hunters on a non-competitive tender and that the Defence Budget would bear this. The Prime Minister agreed to this amendment.
- (iii) It had been suggested that an additional paragraph should be inserted after paragraph 4 to make clear that there would also be an adverse effect on the receipts of privatisation of Yarrow; and that, to contain this, a public assurance should be given that the Type 23/03 contract would be let on the outcome of a competitive tendering process. The Prime Minister agreed to this amendment.



The Prime Minister authorised you to circulate the note to members of the Cabinet under a minute indicating that, unless Cabinet Ministers let you know to the contrary by early next week, she would assume that the proposal was agreed.

F.R.B.

25 January 1985

B  
NBPM

70 WHITEHALL, LONDON SW1A 2AS

01-233 8319

*From the Secretary of the Cabinet and Head of the Home Civil Service*

Sir Robert Armstrong GCB CVO

Ref. A085/262

LORD CHANCELLOR

Orders for Frigates

Since this matter was considered in Cabinet yesterday there have been further discussions with the Secretaries of State concerned, which have resulted in a new proposal which was not among the options considered by the Cabinet but which would meet the strongly felt wish of the Cabinet that there should be further work for Cammell Laird.

2. The Prime Minister has instructed me to send you the attached note, which describes the new proposal. You will see that it is agreed between the Secretaries of State concerned and with the Lord President and the Chancellor of the Exchequer, and commended by the Prime Minister to her colleagues.

3. I am sending copies of this minute and the note to other members of the Cabinet. If I have not heard otherwise by noon on Monday 28 January, I shall assume that you and they are content that this proposal should be put into effect.

4. I am also sending copies of this minute and the note to the Chief Whip and the Paymaster General.

Robert Armstrong

25 January 1985

ORDER FOR FRIGATESNote by the Secretary of the Cabinet

At its meeting on 21 January the Cabinet asked that further consideration should be given to possibilities of placing orders for further work with Cammell Laird (CL), so as to ensure its continued operation, consistently with confirming orders to Swan Hunter (SH) for the provision of two frigates.

2. The Secretaries of State for Defence and Trade and Industry have agreed upon the following proposal:

(1) One of the two orders for Type 22 frigates (Type 22/13) should be placed with CL and the other (Type 22/14) with SH.

(2) The Ministry of Defence has embarked upon a programme for the construction of Type 23 frigates. The first (Type 23/01) has been ordered from Yarrow; the next two are due to be put out to tender in a year's time. Both were to be put out to competitive tender. It is now proposed that it should be decided and announced now that one (Type 23/02) will be ordered from SH. The other (Type 23/03) will be put out to competitive tender.

(3) The Secretary of State for Defence will instruct the Accounting Officer for the Ministry of Defence Procurement Vote to accept the CL tender for one Type 22 frigate and to place the contract for one Type 23 frigate with SH on a single tender, subject to satisfactory agreement on price and other contract terms.

(4) The Secretary of State for Defence will absorb in the Defence Budget the extra direct costs (£7 million) of ordering Type 22/13 from CL rather than from SH, and the cost of whatever cash injection into CL is required to keep open the option to privatise CL. The amount required for this purpose is to be agreed between the Secretary of State for Defence, the Secretary of State for Trade and Industry and the Treasury. There is already provision for Type 23/02 in the approved Public Expenditure Survey programmes for the Defence Budget; the Defence Budget will also absorb any additional costs that may result from letting the Type 23/02 contract to SH on non-competitive tender.

3. The value of the Type 23/02 frigate order to SH will be of the order of £70 million during the period of construction beginning about April 1986; the value of the second Type 22 frigate order to SH would have been of the order of £90 million during the period of construction beginning about April 1985. The penalty to SH is thus a reduction of £20 million in the value

of the order and a delay of about a year in its timing. This is likely to mean some redundancies at SH in 1985, over and above the 500 which they are likely to have to declare in any case, and may marginally reduce the proceeds of privatising SH; but these effects will be nowhere near as great as would have to be faced if SH were not assured of the order for Type 23/02.

4. There will be certain indirect costs of this proposal - extra losses of some £1½ million at SH and £5 million at CL - which will add some £6½ million to the External Financing Limits of British Shipbuilders (BS) in 1985-86.

5. It is understood that as a result of this proposal there will be an adverse effect on the receipts of the Yarrow privatisation. This is not easily quantified, but will be of the order of £5-10 million. This will entail a corresponding further adjustment to the External Financing Limits of BS. In order to contain this, it will be necessary to give a public assurance that the Type 23/03 contract will be let on the outcome of a fair competitive tendering process.

6. This proposal has been agreed with the Lord President of the Council and the Chancellor of the Exchequer.

7. The Prime Minister would be content to resolve the matter on the basis of the proposal set out in this note, and commends it to her colleagues accordingly.

ROBERT ARMSTRONG

Cabinet Office

25 January 1985



10 DOWNING STREET

Prime Minister ①

RTA has set out the  
proposals for frigates agreed  
last evening.

Robin thought that in  
addition to to £7 milia  
and the cost injection into  
C-C being borne by the  
Reference Budget, it would  
meet the losses of the two  
yards, i.e. £6½ milia. At  
the point I left to meet by  
this last item was not  
included.

Agree as drafted? Yes  
no

or Agree including £6½ milia  
to be met by Reference Budget?

AT  
24/1



Ref. A085/258

PRIME MINISTEROrders for Frigates

--- I attach a note setting out the proposal which you agreed with the Lord President, the Chancellor of the Exchequer and the Secretaries of State for Defence and Trade and Industry this evening.

2. I am sending copies of this minute and the note to those Ministers. If tomorrow morning it is confirmed that you and they are content that it correctly records the proposal, the note will be used as the basis for informing other members of the Cabinet what has been agreed. We shall try to complete that process during the course of tomorrow. Assuming that other members of the Cabinet concur, the Secretary of State for Defence will make an announcement in Parliament next week.

for ROBERT ARMSTRONG

24 January 1985

ORDERS FOR FRIGATES

Note by the Secretary of the Cabinet

At its meeting on 21 January the Cabinet asked that further consideration should be given to possibilities of placing orders for further work with Cammell Laird (CL), so as to ensure its continued operation, consistently with confirming orders to Swan Hunter (SH) for the provision of two frigates.

2. The Secretaries of State for Defence and Trade and Industry have agreed upon the following proposal:

(1) One of the two orders for Type 22 frigates (Type 22/13) should be placed with CL and the other (Type 22/14) with SH.

(2) The Ministry of Defence has embarked upon a programme for the construction of Type 23 frigates. The first (Type 23/01) has been ordered from Yarrow; the next two are due to be put out to tender in a year's time. Both were to be put out to competitive tender. It is now proposed that it should be decided and announced now that one (Type 23/02) will be ordered from SH. The other (Type 23/03) will be put out to competitive tender.

(3) The Secretary of State for Defence will instruct the Accounting Officer for the Ministry of Defence Procurement Vote to accept the CL tender for one Type 22 frigate and to place the contract for one Type 23 frigate with SH on a single tender, subject to satisfactory agreement on price and other contract terms.

(4) The Secretary of State for Defence will absorb in the Defence Budget the extra direct costs (£7 million) of ordering Type 22/13 from CL rather than from SH, and the cost of whatever cash injection into CL is required to keep open the option to privatise CL. The amount required for this purpose is to be agreed between the Secretary of State for Defence, the Secretary of State for Trade and Industry and the Treasury.

3. The value of the Type 23/02 frigate order to SH will be of the order of £70 million during the period of construction beginning about April 1986; the value of the second Type 22 frigate order to SH would have been of the order of £90 million during the period of construction beginning about April 1985. The penalty to SH is thus a reduction of £20 million in the value of the order and a delay of about a year in its timing. This is likely to mean some redundancies at SH in 1985, over and above the 500 which they are likely to have to declare in any case, and may marginally reduce the proceeds of privatising SH; but these effects will be nowhere near as great as would have to be faced if SH were not assured of the order for Type 23/02.

4. There will be some addition to the External Financing Limits of British Shipbuilders as a result of this proposal: this addition could amount to some £6½ million in 1985/86.
5. This proposal has been agreed with the Chancellor of the Exchequer and the Lord President of the Council.
6. The Prime Minister would be content to resolve the matter on the basis of the proposal set out in this note, and commends it to her colleagues accordingly.

24 January 1985



Ref. A085/241

PRIME MINISTER  
\_\_\_\_\_Type 22 Frigates

C(85) 3

## BACKGROUND

B \_\_\_\_\_ Cabinet decided on 19 July 1984 (CC(84) 27th Conclusions, Minute 5) that there should be a third round of tendering for the two Type 22 frigates required by the Ministry of Defence. This decision took into account the fact that the earlier tender submitted by Cammell Laird overestimated the extent to which that yard's overhead costs would be recovered from other work, and the problems created by the industrial disruption then occurring at Cammell Laird. The lowest third round tender was submitted by Swan Hunter, but the Secretary of State for Defence nevertheless proposed in this 18 December 1984 minute that one of the two orders should be placed with Cammell Laird. The Secretary of State for the Environment endorsed this judgment in his minute of 18 January 1985. The Secretary of State for Trade and Industry pointed out the difficulties arising from not accepting the lowest tender in his minute of 21 December 1984. The note by officials of the Department of Trade and Industry, Treasury and the No 10 Policy Unit attached to the Secretary of State for Trade and Industry's paper (C(85) 3) sets out the facts the Cabinet will need to bear in mind in deciding which yards are to receive the frigate orders.

C \_\_\_\_\_

D \_\_\_\_\_

E \_\_\_\_\_

## MAIN ISSUES

2. The main issues before the Cabinet are as follows -
- a. Should Swan Hunter receive both orders, or should one order be placed with Cammell Laird despite the need for a Ministerial direction to the Ministry of Defence Accounting Officer to this effect?
  - b. If one of the orders is placed with Cammell Laird, how should the additional costs to British Shipbuilders (BS), over and above the additional direct costs to the Ministry of Defence, be met?
  - c. If both the orders are placed with Swan Hunter, what steps if any should be taken to keep Cammell Laird in operation, at least for a limited period?

Costs

3. The additional costs of dividing the orders between the two yards are summarised in paragraph 9 of the note by officials. Ignoring the items in the comparison which roughly balance each other, there is an extra cost of some £47 million in the course recommended by Mr Heseltine (£7 million extra cost to the Ministry of Defence, an extra cost to BS of about £20 million for a cash injection to Cammell Laird and a loss of a further £20 million in reduced receipts from warshipbuilding privatisation).

x be £47 million for no net increase in jobs and £39,000 for each of the 1200 jobs transferred from Tyneside to Merseyside. Is this too high a price even to reward moderates?

AT

Arguments For and Against Splitting the Orders

4. Arguments in favour of giving one of the orders to Cammell Laird are:

- a. The good sense of the Cammell Laird workforce in overcoming industrial disruption deserves to be rewarded.
- b. The problems of Merseyside deserve special treatment.
- c. Cammell Laird should receive some benefit from having been the lowest tender in the first two tendering rounds. (Mr Heseltine is particularly critical of the fact that BS refused to allow Cammell Laird to tender for both orders on the third round, because redundancies there since last summer had deprived that yard of the capacity to build more than one vessel).

The counter-arguments in favour of Swan Hunter are -

- a. That yard's productivity and industrial relations record is substantially better than Cammell Laird's.
- b. Unemployment on Tyneside is now lower than on Merseyside. Protecting jobs on Merseyside through a Type 22 order would result in an exactly corresponding loss of jobs on Tyneside.

Responsibility for BS Additional Costs

5. If Cammell Laird were to receive one of the orders, Mr Tebbit is likely to argue that the Defence budget should be responsible not only for the total cost of the frigates, including any over-run, but also for the cash injections which would be needed at Cammell Laird (see paragraph 4 of his minute

of 21 December 1984). He will say that BS cannot be expected to bear the extra costs of the Cammell Laird cash injection within the very tight external financing limit in prospect for them.

#### Other Measures to Help Cammell Laird

6. The Ministry of Defence were earlier contemplating a major refit for the Balder London, which would have employed 300 people at Cammell Laird for a year at an extra cost (ie over and above the price to be expected through competitive tendering) of £2-3 million. They are not at present intending to go ahead with this, and have not been able to identify any further comparable work which, together with the Balder London, would make it possible to provide continuing employment for half the yard's projected workforce (500 redundancies are already in prospect out of the 1700 workers currently employed). Failing defence contracts, it might be possible for BS to secure sufficient civil work to keep the yard operating for another year, at the cost of an effective subsidy of £6-10 million. This would then provide an opportunity to sell the yard as a going concern, although this would almost certainly be more expensive than closing it down and then selling it as a facility without the workforce. If Cabinet agree that both orders should go to Swan Hunter, they may wish to ask the Department of Trade and Industry to consider urgently, together with the Ministry of Defence and the Treasury, what would be involved in securing sufficient work to keep Cammell Laird going for a further year and then selling it as a going concern (although not as a warshipbuilding yard).

#### HANDLING

7. You may like to invite the Secretary of State for Defence to speak first, since the substantive proposal before the Cabinet is that in his minute of 18 December 1984. The Secretary of State for the Environment will probably wish to



speak in his support. The Secretary of State for Trade and Industry, who has already made his views clear in his minute of 21 December 1984 could be asked to speak next. The Chief Secretary, Treasury will also wish to give his views about how the costs of the alternative courses might be met.

CONCLUSIONS

8. You will wish the Cabinet to reach conclusions on the following:
- a. the destination of the two Type 22 Frigate orders;
  - b. if one order goes to Cammell Laird, the responsibility for the resulting additional costs to BS;
  - c. if both orders go to Swan Hunter, possible alternative measures to keep Cammell Laird in operation pending its sale as a going concern.

RA

ROBERT ARMSTRONG

23 January 1985

PRIME MINISTER

23 January 1985

TYPE 22 FRIGATES

Whatever the previous history on this order the note by officials (DTI, Treasury and Policy Unit) sets out the current facts. MOD officials were also involved in drawing up the note and do not dispute its content.

One T22 frigate order is to go to Swan Hunter. The issue is whether they also get the second one or whether Government intervenes within British Shipbuilders and directs it to Cammell Laird at an immediate extra cost of £7 million.

1,200 jobs will be lost by the yard that misses out. Unemployment in Birkenhead is at the same level as Newcastle. If the order goes to Swan Hunter then Cammell Laird should close and be sold off as a facility. But if Cammell Laird get the order then Government will face further additional costs of at least £40 million split equally by way of reduced privatisation proceeds at Swan Hunter and, de facto, a continuing overhead burden at Cammell Laird.

Both workforces have come under heavy union pressure to fight the large compulsory redundancies that have affected their yards. The Swan Hunter workforce has overridden the union from the start whereas the Cammell Laird one waited for the 37 sitters-in to be arrested before the Back to Work Committee took them across the picket line. Will Government signal a better message towards union moderation by backing the prodigal son or the one that resisted temptation?

British industry has been blighted by stubborn workforces which only accept change when it is too late. Closure of Cammell Laird is a bitter pill but it would allow the vital message to be made that militancy must be resisted from the

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start and not only when it has so undermined viability as to be obvious to everyone. After all, if Cammell Laird did get a T22 the militants would claim it was because of the sit-in. What's more, they would be right!

Michael Heseltine has argued that because Cammell Laird were only allowed to bid for one ship their overheads were inevitably loaded against them. In fact, like all BS yards, Cammells were allowed to assume that the rest of the yard would effectively be fully employed and so no excess overhead is reflected in the price. This is confirmed by only a £2 million difference in the quotes of each of the yards for a single frigate.

BS only let Cammells bid for one T22 because by that stage to give them both orders would have required them to recruit a further 800 men whilst sacking an additional 800 men at Swan Hunter. This would clearly have been wrong.

However, the question is not just the £7 million difference in the tenders, it is whether it can be worth spending £47 million plus to shift 1,200 redundancies from Newcastle to Birkenhead so as to reward the belated Back to Work move: but which is equally likely to give the militants an excuse to claim the credit and that the sit-in on HMS Edinburgh worked. We therefore recommend that both T22 orders go to Swan Hunter.

The compromise of finding other work for Cammell Laird (Balder London and possibly a submarine) would be expensive although much less so than giving them a T22. If Cammell Laird were then sold with this limited workload it might survive; just as from very similar circumstances Scott Lithgow still has chances of winning through.

Peter Warry  
PETER WARRY

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COMMERCIAL IN CONFIDENCE

*BT // To account PU response*  
*AT 23/1* *ce 100*



DEPARTMENT OF TRADE AND INDUSTRY  
1-19 VICTORIA STREET  
LONDON SW1H 0ET 5422  
TELEPHONE DIRECT LINE 01-215  
SWITCHBOARD 01-215 7877

Secretary of State for Trade and Industry

23 January 1985

Rt Hon Michael Heseltine MP  
Secretary of State for Defence  
Ministry of Defence  
Main Building  
Whitehall  
SW1A 2HB

*D Michael*

WARSHIPBUILDING PRIVITISATION: TRAFALGAR HOUSE INTEREST IN YARROW AND VICKERS SHIPBUILDING AND ENGINEERING LTD (VSEL)

I am writing to seek your agreement to the line I propose to take with Trafalgar House who are seeking guidance as to whether I would be likely to withhold my consent under the Aircraft and Shipbuilding Industries Act to a sale by British Shipbuilders to them of VSEL if they had already acquired Yarrow. They are interested in acquiring both companies but their main interest is in VSEL which is coming on to the market later than Yarrow, for which bids are due in by 15 February.

2 For a number of reasons, I am keen to give as much encouragement as possible to Trafalgar House's interest in the warship yards. I therefore propose to tell them that if they acquire Yarrow, they will not be debarred from bidding for VSEL. If, however, there is a close contest for VSEL I will in deciding whether to give my consent to a particular sale, take account of all the relevant factors at the time including the effects of competition.

3 The only potential problem about Trafalgar House ownership of VSEL is that they already own Scott Lithgow, who along with Cammell Laird and Yarrow are bidding to your Department for the second submarine line for conventional submarines (worth some £65m per submarine to the builder). Although bids have not yet been received, I understand that Scott Lithgow are more likely to be successful than Yarrow. Even so, I understand also that your officials are concerned about the possibility of Trafalgar House ownership of both VSEL and the winner of the competition for the second submarine line whether it is Yarrow or Scott Lithgow.

4 While I accept that there is a risk that Trafalgar House

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ownership of VSEL as well as Scott Lithgow could allow us to miss the opportunity for a small but real increase in competition for conventional submarines for MOD, I am strongly of the view that Trafalgar House should not be discouraged from bidding for both Yarrow and VSEL. This is for three main reasons:

(a) at present, the only sure competition for Yarrow is an employee buy-out bid which appears to be having difficulty raising sufficient cash. The only sure competition for VSEL is a bid from GEC, possibly in conjunction with a British Aerospace bid. In the case of VSEL, Lazard's estimate a sale price of £50-£55m, well below the £100m by way of PDC which the Government will have invested in the Submarine Facility by 31 March 1986. Unless both these bids face real competition from a bidder with real financial strength, the proceeds are likely to be so derisory as to make the privatisation of the warship yards seem politically inept, unless;

(b) we are forced back to the wholesale flotation of the warship yards as a whole; in which case there will be no real competition for MOD orders unless they seek foreign competition. We will have thus replaced a public sector monopoly with a private sector monopoly and will have reduced competition since a private sector company is unlikely to adopt as relaxed an attitude as British Shipbuilders to competition between yards;

(c) there is a good industrial case for Trafalgar House to buy Yarrow to help out at Scott Lithgow which lost many of its best technical personnel in the period prior to its privatisation. Trafalgar House would use personnel from Yarrow to rebuild Scott Lithgow's technical expertise especially for MOD work.

5 I believe therefore that we should give every encouragement to Trafalgar House's interest in both Yarrow and VSEL. If in the event there is a close contest for VSEL between GEC/British Aerospace and Trafalgar House we will need to decide in light of all the factors at the time, including the effects on competition, whether we prefer to go to the second bidder. GEC/British Aerospace ownership of VSEL could in itself cause concern about the degree to which GEC, British Aerospace and VSEL between them are customers of MOD.

6 I should be grateful for your views and those of colleagues by Friday 25 January. I am copying this letter to the Prime Minister, other members of E(A) and Sir Robert Armstrong.

NORMAN TEBBIT

JH1BSV

23 JAN 1985

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CONFIDENTIAL

Prime Minister

✓ CNO

Although Mr Tebbit is proposing no action, he is bringing this to your attention as it is relevant to the decision to allocate work on Type 22 frigates to Messenyside in the North East

PRIME MINISTER

AT 28/1

AUSTIN AND PICKERSGILL

You and Cabinet colleagues should be aware that British Shipbuilders (BS) may shortly have to declare some 675 lay-offs at Austin and Pickersgill in Sunderland. These lay-offs will need to be converted to redundancies by about April when Austin and Pickersgill may close unless they are able to secure new orders by then. It seems increasingly unlikely that they will be able to find such orders.

2 This would be a further severe blow to shipbuilding in the North East (as you know Swan Hunter on the Tyne are in the process of making 2,100 workers redundant). I do not however propose that either my Department or BS should do more than we are currently doing to find new work for Austin and Pickersgill. There are only three prospects for major orders:

the first, from a German owner who is currently demanding terms greater than BS are prepared to pay under the financial limits we have set them following E(A)'s agreement last summer that we should set BS's merchant order intake on a downward glidepath;

the second, from Ethiopia, for which there is inadequate ECGD cover. The official Export Guarantee Committee has recommended against extending the s.2 country limit. BS are exploring alternative financial packages, but the prospects for success do not look good;

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the third, a possible order from ODA for a ship for St Helena, but it seems likely that a smaller ship will be required than could sensibly be built at Austin and Pickersgill. In any case OD will not be ready to take a decision for some time.

3 Austin and Pickersgill currently employs 1,827 people. If they were to close, some might be employed by Sunderland Shipbuilders but the rest would probably become redundant.

4 I am copying this minute to members of the Cabinet, to the Chief Whip and the Paymaster General, and to Sir Robert Armstrong.

N7

N T

22 January 1985

Department of Trade and Industry

JH4ASG

MAIL  
COMMISSION

23 JAN 1985

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File DA

10 DOWNING STREET

*From the Principal Private Secretary*

MR. GREGSON  
CABINET OFFICE

Type 22 Frigates

The Prime Minister has seen your minute of 18 January to Mr. Turnbull (P.01475) and she has agreed that the note by officials on Type 22 Frigates should be circulated to Cabinet under cover of a note by the Secretary of the Cabinet on the Prime Minister's instructions if Mr. Tebbit does not circulate it himself. The Prime Minister has pointed out that the Secretary of State for Defence may challenge the basis of the figures in paragraph 3 of the attachment on the grounds that the terms of the tender allowed other tenderers to spread their overheads by bidding for both ships but did not allow Cammell Laird to do so since they tendered only for one.

You may like to take account of this point in the Prime Minister's brief for the discussions.

RAS

21 January 1985

CONFIDENTIAL

ho

DEPARTMENT OF EMPLOYMENT



Caxton House  
Tothill Street  
London SW1H 9NF  
Telephone 01-213 - 6670

Andrew Turnbull, Esq.

WITH THE COMPLIMENTS OF  
THE PRIVATE SECRETARY TO THE PARLIAMENTARY  
UNDER SECRETARY OF STATE

Mr. Bottomley has asked me  
to send you these letters for  
the Prime Minister, re Connell Laird.

Jeremy Cooper

23.1.85

<sup>auew</sup>  
**tass**

**CONFIDENTIAL**

RECEIVED  
27 JAN 1985  
DEPT OF EMPLOYMENT

NBRM  
AT  
23/1

**KEN GILL** - General Secretary

Telephone: 01-948 2271

OUR REF. ....  
YOUR REF. ....  
ENCLOSURES .....

Please confine each letter to one subject

141 Plymyard Avenue,  
Eastham,  
Wirral,  
Merseyside, L62 8EJ.

Mr. Peter J. Bottomley M.P.,  
Department of Employment,  
Caxton house,  
Toxhill Street,  
Westminster,  
London, SW1.

18th January 1984

cc M.P. Smith  
PS/M. Manson  
PS/M. Clark  
NYK 22.1

Dear Peter,

We at Cammell Laird were informed, correctly or incorrectly, that the final decision on where the Type 22 contracts are placed will be made by the Cabinet. Acting on this information, the C.S.E.U. Shop Stewards Committee decided to write to Mrs. Thatcher, Cabinet Ministers and M.P.s with a possible interest in our cause. The text of the letter enclosed to you was used in each case.

There are two points I would like to make which the stewards themselves have left out. The full time union officials and the C.S.E.U. full time representatives in this area are totally opposed to the recently elected stewards in Cammell Laird. They are backing the militant movement here on Merseyside. The stewards elected by G.M.B.A.T.U. members are in the process of having their credentials removed by their local union office. The full time officials of G.M.B.A.T.U. say that every member entering this yard will eventually be disciplined by the union. Names are being recorded at our gates by militants as our workforce arrives. The D.C. of my own union TASS are trying to close our Management Branch because they consider our actions are, in their words, despicable. Local full time officials of other unions refuse to enter our yard or have anything to do with the elected stewards. The national officials do not in general seem to fully support this local action, but they will do nothing to resolve the split. I consider that they intend to sit and wait for the defeat of one side or the other. My great fear is, with special reference to the hourly paid, that if we fail to obtain an order high levels of redundancy or even closure could occur. These very men now making a stand against the union militants would be barred by union interference in ever obtaining another job on Merseyside.

1.

/contd.....



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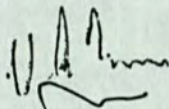


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2.

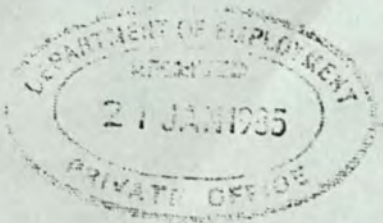
We are faced with two competitors with reference to the pending Type 22 contracts. Vospers never involved themselves in our disputes. On this account I would not comment on their ability concerning a contract. They, like ourselves, will put their case to Government. Swan Hunter, in a mercenary manner, sent coachloads of pickets and substantial amounts of money to our strikers against the wishes of the majority. At our Tynemouth Conference last month their representatives slated us publicly because of our moderate attitude over redundancy. They spearheaded the call for national action against enforced redundancy and privatisation. Swan Hunter made it clear that by a ballot vote of the total workforce 72% favoured action. They stated in no uncertain terms that they would not take the soft line of Cammell Laird but would fight even if other yards refused. We consider with such a large workforce even the two Type 22 contracts would not stop some redundancy at Swan Hunter. With their present attitude we believe, if awarded, these orders would be quickly converted to the sword with which to enforce their wishes.

Yours sincerely,



W.A. MORRIS  
Chairman  
TASS Merseyside Management Branch

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C.S.E.U. Shop Stewards Committee,  
Cammell Laird Shipbuilders Limited,  
New Chester Road,  
Birkenhead,  
Merseyside, L41 9BP.

Mr. Peter J. Bottomley M.P.,  
Department of Employment,  
Caxton House,  
Toxhill Street,  
Westminster,  
London, SW1.

17th January 1985

Dear Mr. Bottomley,

Cammell Laird Shipbuilders Limited

The decision by Government, at the end of last month, to postpone the placing of the Type 22 contracts until the end of January was met with a little dismay by our workforce. With work now running out, short time working has been instigated. As there has been such a long time lapse since our Back-to-Work Committee met members of government at your conference we considered it advisable to give you a progress report.

With the return to work, new elections for shop stewards were held in the shipyard. A number of the Back-to-Work Committee stood and were elected. The Back-to-Work Committee held its final meeting at the beginning of this month and agreed that its aims had been met. It was agreed that following the new elections it had every faith in the stewards and their aspirations. It was unanimously agreed by the Back-to-Work committee that the time had come to disband and hand over to the elected representatives. We thank them for the effort put in on behalf of the workforce and their confidence in us.

Some pickets are still at our gates every morning with their slogans and anti-government propaganda. They are unable to prevent any of the workforce from entering the yard.

British Gas made some rather derogatory statements in the press and on radio and T.V. last week with reference to the late delivery (now 12 months) of their jack-up rig. They suggested that the extra costs involved in hiring a replacement rig should be covered by Cammell Laird. We viewed their comments with grave concern and have decided to comment on the charges.

Three factors contributed to the extension of the contract which British Gas seem to have overlooked:

1. Jacking Equipment produced by a Sub-Contractor was delivered 10 months late. These major items of equipment adjust and position the legs when in service. Cammell Laird is claiming an extension of 28 weeks to the original delivery date as a direct consequence of this late delivery.

2. The dispute, involving 37 men, stopped work for 16 weeks in total. The details of this dispute have been made known to Government so no further comments are required. Cammell Laird are claiming the full sixteen weeks as a further extension.
3. After the start of the contract changes on the leg footings were required. It is estimated that this added a further four weeks work plus time involved in towing the rig to France for drydocking to enable the new footings to be fitted. (Cammell Laird dry docks being unsuitable).

We consider that our workforce cannot be held to blame in total for the problems involved on the British Gas contract. We would ask that when a decision is made, with reference to the pending Type 22 contracts, the three points tabled be taken into account. It must also be remembered that this contract was only the second offshore structure and the first of this type constructed by our company. Many lessons had to be learned by all.

With reference to industrial relations within the yard a new understanding between workforce and management exists. It is jointly agreed that the old hard-line attitudes are out and a more tolerant and constructive approach will be made to problems in the future. The aim being fair and amicable settlements which satisfy both sides without confrontation from either. The hourly-paid, staff and management representatives now hold collective meetings on topics of joint interest. Information and assistance is freely exchanged between the three groups. Major decisions are no longer made by stewards alone but referred back to mass meetings attended by all groups. As stewards we consider this new approach to be in the best interests of the members we represent.

The militants on Merseyside still endeavour by one means or another to influence and intimidate our workforce. The workforce in return totally reject their demands and approaches. After meeting with us the Tugboatmen reversed their decision and supported our claims. They moved the Type 42 Destroyer and launched our rig. Merseyside desperately needs a Type 22 order to prove that moderation produces results. The militants are equally desperate for the order to go elsewhere. To them the lost order would re-vitalise their rapidly reducing support in this area. They need to prove that militant actions are the only effective way to influence Government.

In the past we have been able to improve on the delivery dates of MOD(N) contracts. We consider that even with our numbers reduced with our increased flexibility this situation will not change. The workforce are genuine when they promise to make every effort to fulfill the requirements of any contracts if awarded to us, within the required timetable.

We consider an order placed on Merseyside would be a devastating blow to the militant movement and it would have favourable repercussions throughout industry in this area.

Yours sincerely,

*Gerry Reeves*

G. REEVES

Secretary - CSEU Shop Stewards Committee  
Cammell Laird Shipbuilders Limited

The attached letter is fully endorsed by all unions within  
Cammell Laird, and counter-signed below:-

C.S.E.U. Officers

*R Pagan* R. PAGAN, Chairman C.S.E.U. Committee : E.E.T.P.U.  
*E Machin* E. MACHIN, Vice C'man C.S.E.U. Committee : A.U.E.W.  
*A Rimmer* A. RIMMER, Treasurer C.S.E.U. Committee : F.T.A.T.

Sub-Committee Shop Stewards

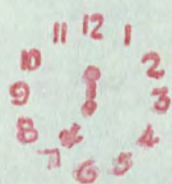
*K Morris* K. MORRIS G.M.B.A.T.U. Chairman A.S.O.B.  
*E Branscombe* E. BRANSCOMBE G.M.B.A.T.U. Secretary G. & M.  
*F Coreless* F. CORELESS E.E.T.P.U. Convener  
*T McCartney* T. MCCARTNEY A.U.E.W. "  
*J Hughes* J. HUGHES T. & G.W.U. "  
*R Burrage* R. BURRAGE U.C.A.T.T. "  
*A Parker* A. PARKER T.A.S.S. (Craft) "

Foremen, Staff and Management

*F Inneli* F. INNELLI G.M.B.A.T.U. Chairman, Foremen's Convener  
*C Boswell* C. BOSWELL T.A.S.S. Secretary, Staff Section  
*A Cotgrave* A. COTGRAVE A.S.T.M.S. Secretary, Management Group  
*D Warkcup* D. WARKCUP S.A.I.M.A. Chairman  
*W Morris* W. MORRIS T.A.S.S. Chairman, Management Group

*Shipboard*

23 JAN 1985





PRIME MINISTER

TYPE 22 FRIGATES AND THE FUTURE OF CAMMELL LAIRD

We are shortly to discuss with Cabinet colleagues the issues raised by Michael Heseltine and Norman Tebbit in their respective minutes of 18/and 21/December, which relate to the selection of shipyards for the construction of replacement Type 22 Frigates.

I regard it as essential that the present workforce at Cammell Laird be maintained at about its present level for two reasons:-

Firstly the Yard currently employs 1700 people, with an estimated further 1200 dependent jobs (sub contractors etc), right at the heart of the Merseyside conurbation. Over 1600 redundancies have already occurred during the last twelve months whilst the Yard has undergone a slimming down and re-structuring process. This has happened in an area which has sustained major job losses over many years (at an accelerating rate in recent years) and where unemployment levels now stand at over 20%. Against this depressing backcloth the Government has committed itself to helping the area tackle its economic, environmental and social problems and when you visited Liverpool in October last year you saw some of the measures we have been taking to bring new hope to the area. Should Cammell Laird close or incur further major job losses the Government's commitment to the area will be questioned because it is seen locally that the Naval orders required to keep the Yard in business are a decision for Government and Government alone.

Secondly, I strongly advocate the need to support the efforts of the 'moderate' workforce which braved vociferous picketing during last year's industrial dispute and 'sit-in'. I met the leaders of the back to work movement after they had succeeded

Time limited  
This will be taken  
at Cabinet next  
week.

CDP  
17/12



in getting the majority of the workforce back into the Yard and had persuaded the relevant unions that the sacked strike ringleaders should not be reinstated. The militants then, and now, are picketing the Yard and telling the shipworkers that their return to work is futile, that the Yard will close anyway and that events in the next few months will prove them right. Failure to place a substantial order to keep the Yard in business would be thrown in the face of the present workforce as evidence that 'moderation does not pay' and that Government assurances about a continuing commitment to the area are hollow gestures. I believe this could have consequences beyond Cammell Laird in other parts of Merseyside and elsewhere.

For these reasons I think it vital that we place a major Naval contract at the Yard to secure existing employment at about its present level. Whether this should be by the building of a Type 22 Frigate or a major refit is perhaps a subsidiary issue. However I think the Yard and its sub-contractors are more closely geared to shipbuilding rather than refitting and I therefore support Michael's proposal to place an order of a Type 22 Frigate.

I am sending copies of this minute to Cabinet colleagues and to Sir Robert Armstrong.

AH Davis

for

P J

18 January 1985

Approved by the Secretary of State  
and signed in his absence



CONFIDENTIAL

P.01475

Prime Minister  
Agree X?

AT  
18/1

MR TURNBULL

TYPE 22 FRIGATES

X | As you will see from Mr Wiggins's minute attached, it seems very likely that the factual note by officials on Type 22 Frigates will be submitted to the Cabinet by the Secretary of State for Trade and Industry (in view of the reluctance of the Secretary of State for Defence to do so). In the much less likely event that Mr Tebbit prefers not to table the note by officials, the only way of bringing it before the Cabinet would be under cover of a note by the Secretary of the Cabinet saying that the Prime Minister had asked him to circulate it. Could you kindly ascertain, on a contingent basis, whether the Prime Minister would be content for this to be done, should it prove necessary?

CONQUEROR

Pg

P L GREGSON

18 January 1985

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1. MR GREGSON <sup>186</sup>
2. MR TURNBULL



cc Mr Dart

TYPE 22 FRIGATES

Cabinet is to discuss the placing of the orders for two Type 22 frigates on 24 January. This question was previously discussed at E(A) on 10 May and 20 June, 1984, and at Cabinet on 19 July 1984.

2. In the first two rounds of tendering, the yard submitting the lowest tenders was Cammell Laird; but these tenders over-estimated the extent to which the yard's overheads could be spread over other work, and it is now clear that had an order been placed with this yard, BS would have incurred a substantial loss. However, before a decision could be taken to place such an order, the yard was occupied by part of the work-force, and Ministers decided that there could be no question of placing public sector orders there for the time being. Despite the continuation of an official 'strike', the occupation has been ended and most of the labour force have returned to work, accepting at the same time substantial redundancies.

3. In accordance with the Cabinet decision of 19 July, there was a third round of tendering for the two frigate orders. On this occasion the lowest tenderer was Swan Hunter, and the natural course would now be for the two orders to be placed with that yard. However, the



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Secretary of State for Defence, having in mind his earlier responsibilities as Minister for Merseyside and also the fact that the Cammell Laird workforce had been encouraged to end their disruption by the prospect of further orders, proposed in his minute of 18 December to the Prime Minister that Swan Hunter and Cammell Laird should receive one order each. (Rationalisation and redundancies which have already occurred at Cammell Laird have eliminated any possibility that the yard could build both frigates).

4. It is hard to resist the conclusion that there is excess capacity in UK warship building yards. Some of this spare capacity may be absorbed by export orders and/or civil work, but the view of most Ministers has been that one yard will have to close if the others are to be successfully privatised. Wherever the orders are placed, 1200 redundancies will be required at one or other yards, although there are some prospects of securing other work as a stop-gap which would postpone at any rate half of these.

5. Leaving aside the prospect of other work, giving both orders to Swan Hunter would mean 1200 redundancies at Cammell Laird; splitting the orders between the two yards would mean 1200 redundancies at Swan Hunter. Splitting the orders would mean an additional £7 million costs directly falling on MOD, with a reduction in the privatisation proceeds from Swan Hunter of about £20 million and a further £20 million required as a cash injection to keep Cammell Laird going. There would also be some additional unrecovered overhead costs at both Cammell Laird and Swan Hunter, which would be roughly equivalent to the net costs of closing Cammell Laird and selling the facility if both orders went to Swan Hunter.



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6. Possible palliative action at Cammell Laird includes the conversion there of the Balder London for MOD at an extra cost (ie. in excess of what would result from a competitive tender) of £2 to £3 million, which would provide work for 300 people for a year. DTI have suggested that a submarine refit could provide work for a similar number for up to two years, at about double this cost - but MOD say they have no such work available. A further possibility would be for BS to offer whatever subsidies were needed to secure some major merchant vessel conversion work for the yard, at the same sort of annual cost.

7. Officials of MOD, DTI, Treasury and the No 10 Policy Unit have prepared the attached note which summarises the facts of the present position. The Secretary of State for Defence has refused to be associated with this note in any way, and insists instead on standing on his minute of 18 December to the Prime Minister. DTI officials expect Mr Tebbit to agree to circulate the note by officials (but omitting any mention of MOD), under cover of a short paper by himself. This would be a convenient way of putting facts before members of the Cabinet.

*JW*

A J WIGGINS

18 January, 1985

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THE ORDER FOR TYPE 22 FRIGATES 13 AND 14  
NOTE BY OFFICIALS

Introduction

1 The purpose of this note is to provide factual background and forecasts bearing on the allocation of the orders for Type 22 frigates 13 and 14. It has been agreed between officials of MOD, Treasury, DTI and the NO 10 Policy Unit. For the most part it concentrates on a comparison of the effect of:

Course (a) placing both orders with Swan Hunter; and

Course (b) splitting the orders between Cammell Laird and Swan Hunter.

Direct Costs

2 In accordance with Cabinet's decision on 19 July 1984, the Ministry of Defence sought fresh tenders for the two ships from Cammell Laird, Swan Hunter, and Vosper Thornycroft. Tenders were returned on 15 September. Swan Hunter and Vosper Thornycroft bid for an order for both ships or either one of them. Cammell Laird tendered for one or other ship but not both. The results of the tendering process may be summarised as follows:

	£m	
2 ships from Swan Hunter	139.4	Course (a)
2 ships from Vosper Thornycroft	140.9	
1 ship from Vosper Thornycroft and 1 from Swan Hunter	145.2	
1 ship from Cammell Laird and 1 from Swan Hunter	145.5	Course (b)
1 ship from cammell Laird and 1 from Vosper Thornycroft	147.2	

In addition, MOD would incur extra costs of about £1M if the order were split. The total extra direct costs of course (b) over course (a) are thus about £7M.

### Indirect Costs

3 When considering indirect costs and redundancies, assumptions need to be made about the level of other work and the allocation of overheads. In providing figures therefore, BS have assumed the same allocation of overheads as was used in the tenders submitted to MOD. Under course (a), unless special action were taken (see para 8 below), BS would close Cammell Laird within two or three months. They would propose to move HMS Edinburgh to another ship-or dock-yard for final fitting out. Under course (b) there would probably be an under-recovery of overheads at Cammell Laird, of some £10m over 1985/6 and 1986/7 together; BS expect Swan Hunter to incur extra under-recovered overheads of £5M in 1985/6 and 1986/7 together with higher figures in later years.

### Redundancies

4 In February, Swan Hunter will employ 5,200 after the current round of 2,100 redundancies is completed. Cammell Laird currently employ 1,700 after implementing 1,600 redundancies in 1984. Both yards are likely to have to declare a further 500 redundancies in 1985 whatever course is chosen.

The yard that does not win the second order will have to declare some 1,200 further redundancies, resulting in Cammell Laird's case in closure. The cost of the 1,200 redundancies will be some £6½M under the Shipbuilding Redundancy Payment Scheme (SRPS).

### Unemployment

5 3 of the 4 Swan Hunter yards are in the Newcastle travel to work area (TTWA). Cammell Laird is in the Wirral and Chester

TTWA. Unemployment rates are as follows:

Average of 12 months  
to December 1984

December 84

Wirral and Chester	17.9%	18.2%
Newcastle	17.9%	18.0%

Unemployment rates in the adjacent TTWAs are as follows  
(1 Swan Hunter yard is in the South Tyneside TTWA):

Liverpool	20.6%
South Tyneside	24.5%

### Industrial Relations

6 In recent years there has been considerable industrial disruption at Cammell Laird. The percentage of man hours lost due to strikes and stoppages at Cammell Laird has been above the BS average. CL has lost over 1.3% of possible man hours each year since 1981/2. It lost nearly 4% in 1983/4. The comparable figures for Swan Hunter have never risen above 0.4%. In July 1984 the Cammell Laird workforce were laid off as a result of industrial action over compulsory redundancies and some of them occupied the work in the yard. 37 sitters-in were jailed in October. As a result of an unofficial Back to Work Committee the workforce on 9 November unanimously rejected a strike call, and over 90% of them are currently at work. At Swan Hunter, the workforce have accepted the current round of redundancies without industrial action and against union advice. Although the "strike" at Cammell Laird remains official, the national union conference (SNC) recently made a low key request to the Minister of State for Industry (Mr Lamont) for a Type 22 frigate order to be placed with Cammell Laird. Both yards have agreed to implement the British Shipbuilders Phase V wage agreement incorporating new working practices.

### Overcapacity

7 As demonstrated in the annex, the current capacity in the UK to build large surface warships is 7 to 8 frigate equivalents a

year against an anticipated MOD requirement for 4 (3 frigates and 1 large auxiliary). The only immediate export prospect is two frigates for Pakistan which Vosper Thornycroft hope to win. MOD will need a second submarine line at a maximum order rate of 1 frigate equivalent. If Yarrow or Cammell Laird were to win the submarine order and Vosper Thornycroft to win the Pakistan order, the available capacity for surface ships would fall to about 6 to 7 frigate equivalents against MOD requirements for 4. If Cammell Laird were to close and be sold as a facility, the capacity immediately available would fall on the same basis to 4 to 5 frigate equivalents, thus largely eliminating the overcapacity. It would be possible however for the new owners of Cammell Laird to attempt to re-enter the warship market.

### Privatisation

8 Under course (a), BS estimate the closure costs to them (ie excluding SRPS) of Cammell Laird would be some £10M; they would then expect to sell Cammell Laird as a facility for a few million pounds. The net costs would be of the order of £5m. Under course (b), Cammell Laird would continue in existence at least for the 4 years required to build the frigate. Even so, because of the anticipated level of losses, and the need for further investment BS and Lazards believe that it could only be privatised if privatisation were accompanied by a cash injection of the order of £20m at least. Course (b) reduces Swan Hunter's profits by some £20m over the period with a comparable effect on privatisation proceeds.

### Special Action for Cammell Laird

9 BS have considered in conjunction with Lazards whether special action at Cammell Laird would improve the position under either course. In particular, they have considered the effect of an award to Cammell Laird on a non-competitive basis of a contract for the conversion of the Balder London which would provide a certain work load for about one year. It could increase MOD's costs by some £2-3m. Under course (a) in BS's view, the award of a Balder London contract would be insufficient to prevent closure of Cammell Laird. However, if a further MOD

contract of a similar size to the Balder London conversion were awarded to Cammell Laird, BS believe that they may be able to sell the yard to someone in the offshore sector preserving at least temporarily up to about 700 jobs. But there can be no certainty that this would provide a future for Cammell Laird and MOD have been unable to identify a suitable potential contract. The costs of such action seem certain to exceed the costs of closure and disposal. Under course (b), the award of a contract for the Balder London would marginally improve the position of Cammell Laird and would defer some 300 redundancies. It would not however make the yard viable and it would only be sold with a very considerable dowry.

Summary comparison of effects of main alternatives

	COURSE (A) (both Frigates at Swan Hunter)	COURSE (B) (1 Frigate at Swan Hunter; 1 at Cammell Laird)
1 <u>Direct Costs</u>	-	Extra costs of £7m to MOD
2 <u>Indirect Costs</u>	-	Extra losses of some £1.5m at Swan Hunter and £5m at Cammell Laird in 1985/6. Effects in later years affect privatisation proceeds.
3 <u>Redundancies</u>	1,200 at Cammell Laird*	1,200 at Swan Hunter*
4 <u>Privatisation</u>	Closure of Cammell Laird and sale as a facility at a net cost of some £5m.	Reduction of Privatisation Proceeds at Swan Hunter of some £20m. Cash injection into Cammell Laird of at least £20m.

16.1.85

\* In addition both yards are likely to have to declare a further 500 redundancies in 1985



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ANNEX

WARSHIPBUILDING CAPACITY

(excluding submarine building at Vickers)

<u>UK Capacity from 1986 (a)</u>	<u>Minimum Capacity</u>	<u>Maximum Possible Capacity</u>
Cammell Laird (b)	1.5	2
Swan Hunter	2.5	2.5
Vosper Thornycroft	0.5	0.5
Yarrow (c)	1.5	2.0
Harland & Wolff (AOR only)	<u>1.0</u>	<u>1.0</u>
	7.0	8.0

Demand (a)

Orders pa  
(average of 1985 - 1990)

Frigates	3	3
AORs	<u>1</u>	<u>1</u>
	4	4

Further demand might be generated from exports, refits, merchant work and second stream submarine building.

Notes

- (a) 1 AOR build time approx = 1 Frigate
- (b) 2 now, decreasing to 1.5 if yard restructured
- (c) 1.5 now, increasing to 2 if module hall built.

DTI  
15 JANUARY 1985

VC



file

10 DOWNING STREET

From the Private Secretary

23 December 1984

Type 22 Frigates

The Prime Minister has noted the Defence Secretary's minute of 18 December about the tendering exercise for the Type 22 Frigates, as well as the Secretary of State for Trade and Industry's comment in his minute of 21 December.

Subject to the views of other colleagues, the Prime Minister thinks that this question will probably have to come back to Cabinet in January. However, she agrees with the Defence Secretary in believing that the courage shown by Cammell-Laird workers in going through picket lines and continuing to work must be recognised.

I am copying this letter to Private Secretaries to members of the Cabinet and to Richard Hatfield in the Cabinet Office.

(C.D. POWELL)

Richard Mottram, Esq.,  
Ministry of Defence.

VC



From the Minister of State for Industry

DEPARTMENT OF TRADE AND INDUSTRY  
1-19 VICTORIA STREET  
LONDON SW1H 0ET

Telephone (Direct dialling) 01-215 5186  
GTN 215  
(Switchboard) 215 7877

~~cc NO~~

NBPM

Dr.

Norman Lamont MP

**CONFIDENTIAL**

The Rt Hon Peter Rees QC MP  
Chief Secretary  
HM Treasury  
Treasury Chambers  
Parliament Street  
LONDON SW1P 3AG

21 December 1984

*Dear Sir*

**BRITISH SHIPBUILDERS - ORDER PROSPECTS, FLEXIBILITY AND CONTROL**

Thank you for your reply to my letter of 27 November agreeing, subject to one point (special credit for export orders), to my proposals for a new financial control and flexibility system for British Shipbuilders.

Financial Control and Flexibility System

I am glad to be able to tell you that, subject to the point on special credit for export orders, I have now agreed the system with Graham Day and it is now in operation. The figures we have agreed will set BS firmly on the path which E(A) agreed in the Summer, and for that reason BS were somewhat reluctant to accept them. With the limits we have set, they cannot altogether rule out the possibility that a major yard will have to close at some point in 1985/6, and that they may therefore not be able, as they had hoped, to complete their regionalisation programme without a major yard closure in this period. I am, however, convinced that the approach we are adopting, of giving the Corporation greater freedom to manage their own affairs within the guidelines we have set, is correct and that the possibility of a yard closure in the period is a necessary risk, especially since I regard the financial limits which we have agreed as being the maximum compatible with the E(A) decision.

THUAJX



### Intervention Fund Aid

You will recall that colleagues agreed that our aim was to secure an Intervention Fund intensity of 30% (plus an additional 5% for Harland & Wolff for certain types of vessels). Mr Andriessen, the outgoing Commissioner for competition, has insisted on a maximum of 20% (though his officials have indicated that something extra would be allowed for Harlands). He said the figure could go up to 30% where there was no competition from any yard in another EC country - but this would be subject to prior Commission approval on a case-by-case basis.

The Commission proposals fall a good way short of what is acceptable. (Unfortunately what we were negotiating for seems to have become public knowledge.) I therefore intend to return to the charge in January after the new Commissioner for competition has taken up his post. That makes it necessary to extend the interim arrangements we have adopted since the last Intervention Fund expired at end-June 1984. These involve (for both BS and the private sector) offering Intervention Fund to yards at a specified level on the understanding that the level that will eventually apply will be no greater than that to which the Commission ultimately agrees and that no monies will actually pass to the yard until this agreement is secured.

As regards Intervention Fund intensities during the interim period, I have told Mr Day, in line with the offer I have already had from Mr Andriessen, that he may assume when necessary an IF intensity of up to 20% where there is EC competition but that for cases involving no competition from within the EC he can assume when necessary an IF intensity of up to 30%. I do not propose to notify such cases to the Commission, but I believe that these arrangements should prove defensible should the Commission challenge them. We would point to the conditional nature of the IF offers and use our reasonable expectation of a better outcome to justify any BS contract losses arising from the assumption of too high an IF level.

### Special Credit for Export Orders

Mr Day argued forcefully that the flexibility which the new financial control system affords BS would be greatly diminished if it did not apply to special credit to export. Most of BS's current order enquiries are for export.

We agreed in 1982 that, although special credit terms more favourable than those contained in the OECD Understanding on credit for ships would be difficult to defend, we could argue if challenged that the international rules in question apply to



Governments and not to commercial undertakings; and that British Shipbuilders like other such undertakings was free to offer its customers credit on terms which need not be constrained by the OECD Understanding (Patrick Jenkin's letter of 7 June 1982 to Douglas Hurd). Although this defence is no less valid for export orders than for home orders, we decided then that in order to minimise the risk of discovery, we would only normally be prepared to permit BS to offer special credit terms for UK owners and that we would need to vet each application. You have of course now agreed that, as part of the new flexibility and control system, BS should have the freedom themselves to offer special credit for UK owners up to 8% NPV.

I think that it would be reasonable to give BS greater freedom for orders for export. Since 1982 we have come to suspect strongly that yards in other Member States have been able to offer credit terms well in excess of the OECD guidelines in cases where they have been in competition with BS, though, in the nature of things, hard evidence is very difficult to obtain. Moreover, under the new control arrangements, the decisions about export credit will be for BS, and the Government will be less directly involved than it would have been hitherto. It is true that the non-involvement argument is not a complete defence since it does not deal with the question of the Government's funding of BS's contract losses but I believe that it is robust enough, and the benefits of giving BS more flexibility important enough, to make the risk worth taking. I therefore propose that where there is no EC competition, BS should be able to offer special credit terms up to 8% NPV. Where there is EC competition however they would need as now to seek our agreement before making any offer. In judging whether special credit is acceptable, our main criterion would be whether the real competition came from EC yards or from elsewhere.

I should be grateful for your early agreement to this.

I am copying this letter to the Prime Minister, Sir Geoffrey Howe, Douglas Hurd, to members of E(A) and to Sir Robert Armstrong.

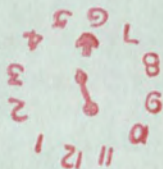
A handwritten signature in cursive script, appearing to read 'Norman Lamont', written in dark ink.

NORMAN LAMONT

THUAJX

NAT IND PT 7

Shipbuilding



71 DEC 1984



E

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21/12/84 C.P. Wainwright

PRIME MINISTER

CAMMELL LAIRD AND TYPE 22 FRIGATES

I have seen Michael Heseltine's minute to you of 18 December proposing to place one Type 22 frigate order with Swan Hunter and one with Cammell Laird.

2 I think we need to look at this proposal very carefully, in the light of the wider implications that will flow from our decision on these orders. I am sure that you will recall that we agreed in Cabinet in July (CC(84)27th meeting) that there should be a further round of tendering for the two Type 22 frigates, on the basis of a realistic assessment of the overheads of the yards involved. As I said at the time, Cammell Laird only "won" the two earlier rounds because they had assumed that overheads would be spread over other work - an assumption that had already proved to be wrong in July, since at that time their management accounts were forecasting a loss of over £7m on the price they were then quoting. Since that time their overheads have in fact come down because of the redundancies they have now put into effect, but unfortunately this has been insufficient to allow them to win other work. Even so, British Shipbuilders (BS) did allow them to assume that they would be allowed to spread their overheads over a large refit contract for MOD for the Balder London (which I understand MOD no longer intend to proceed with) and a large amount of unspecified work equivalent to a Type 2400 submarine and the third AOR vessel. Despite misgivings, BS also allowed them to assume a saving in overheads of £1.4m per annum from a priority based budgeting exercise.

JH3BHL



3 It is true that BS did not allow Cammell Laird to bid for both Type 22 frigates in the latest round of tenders, because they could not do both with their reduced labour force (1700) without recruiting 800 extra workers. This would obviously not be sensible when there is patent overcapacity in this sector. Both Swan Hunter and Vosper Thornycroft have already had to declare redundancies recently (2,100 and 790 respectively) and both yards will have to declare more if they are unsuccessful. That is, BS would have to fire 800 men in the North-East or on the south coast in order to re-employ 800 men on Merseyside, which I do not find an attractive or an economic proposition.

4 I cannot therefore accept in any way the suggestion that the current round of tendering has been fixed. The process which Cabinet asked to be set in hand has been completed. The straightforward solution would be to accept the result and place both orders with Swan Hunter forthwith, at a considerable saving (some £6m) to the Defence vote and avoiding even greater additional costs to British Shipbuilders; the latter I assume Michael would also wish to carry on his budget.

5 In addition to the arguments about which tenders are the cheapest - which are of course ultimately for Michael - there are other financial implications flowing from the placing of these orders which are of concern to me. Michael's proposal would add significantly to BS's costs through increased under-recovery of overheads and the likely reduction in privatisation proceeds. It would certainly directly depress the sale price of Swan Hunter, and - since the award of a Type 22 frigate to Cammell Laird would manifestly leave the overcapacity problem unresolved - would indirectly affect the sale price of all the yards making large surface ships. I am





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not yet in a position to quantify the effects, but they would be likely to exceed by several times the direct difference in tender prices. It would hardly be right that any such extra costs to BS should be borne by DTI.

6 Aside from the question of costs, there is also the effect of a decision to place an order with Cammell Laird on the workforces of Swan Hunter and Vosper Thornycroft against the outcome of the tender process. Not only would such a decision be quite unfair and a poor reward for the loyalty and continuing moderation of the entire workforces at both yards in the face of large scale redundancies, but in Swan Hunter's case it should be recognised that unemployment in Tyne and Wear is as high as it is on Merseyside.

7 I should, however, make it clear that I am not opposed to considering with Michael some other action in favour of Cammell Laird if colleagues feel it is necessary to do so, either because of the general situation on Merseyside or because of the efforts of the Back to Work Committee. But any such action would need to be less damaging to the other yards and their workforces than the placing of an order there for a Type 22 frigate.

8 It is possible, even without an order, that someone (possibly from the offshore industry) might buy Cammell Laird as a going concern, but this is far from certain. The chances of disposing of Cammell Laird as a going concern would certainly be improved if they had a workload to tide them over while a new owner finds new work. Perhaps the best way to do this would be for MOD to place with the yard an order for a refit on a non-competitive basis.

9 Such a solution should be considerably cheaper and less

JH3BHL



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damaging to our broader plans for shipbuilding than the one proposed by Michael, and would offer a real prospect of a future for at least some of the workforce at Cammell Laird.

10 I hope that you and colleagues will agree that we should discuss the matter after the holiday.

11 I am sending copies of this minute to the members of the Cabinet and to Sir Robert Armstrong.

*momentarily*  
*PP*

N T

21 December 1984

*Seen and approved by the  
Secretary of State, and  
signed in his enforced absence*

Department of Trade and Industry

JH3BHL

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21 DEC 1984

11 12 1 2 3 4 5  
6 7 8 9 10



PRIME MINISTER

TYPE 22 FRIGATES AND THE FUTURE OF CAMMELL LAIRD

We are shortly to discuss with Cabinet colleagues the issues raised by Michael Heseltine and Norman Tebbit in their respective minutes of 18 and 21 December, which relate to the selection of shipyards for the construction of replacement Type 22 Frigates.

I regard it as essential that the present workforce at Cammell Laird be maintained at about its present level for two reasons:-

Firstly the Yard currently employs 1700 people, with an estimated further 1200 dependent jobs (sub contractors etc), right at the heart of the Merseyside conurbation. Over 1600 redundancies have already occurred during the last twelve months whilst the Yard has undergone a slimming down and re-structuring process. This has happened in an area which has sustained major job losses over many years (at an accelerating rate in recent years) and where unemployment levels now stand at over 20%. Against this depressing backcloth the Government has committed itself to helping the area tackle its economic, environmental and social problems and when you visited Liverpool in October last year you saw some of the measures we have been taking to bring new hope to the area. Should Cammell Laird close or incur further major job losses the Government's commitment to the area will be questioned because it is seen locally that the Naval orders required to keep the Yard in business are a decision for Government and Government alone.

Secondly, I strongly advocate the need to support the efforts of the 'moderate' workforce which braved vociferous picketing during last year's industrial dispute and 'sit-in'. I met the leaders of the back to work movement after they had succeeded

Prime Minister  
This will be taken  
at Cabinet next  
week.

CDP  
15/1

c PLY ②



in getting the majority of the workforce back into the Yard and had persuaded the relevant unions that the sacked strike ringleaders should not be reinstated. The militants then, and now, are picketing the Yard and telling the shipworkers that their return to work is futile, that the Yard will close anyway and that events in the next few months will prove them right. Failure to place a substantial order to keep the Yard in business would be thrown in the face of the present workforce as evidence that 'moderation does not pay' and that Government assurances about a continuing commitment to the area are hollow gestures. I believe this could have consequences beyond Cammell Laird in other parts of Merseyside and elsewhere.

For these reasons I think it vital that we place a major Naval contract at the Yard to secure existing employment at about its present level. Whether this should be by the building of a Type 22 Frigate or a major refit is perhaps a subsidiary issue. However I think the Yard and its sub-contractors are more closely geared to shipbuilding rather than refitting and I therefore support Michael's proposal to place an order of a Type 22 Frigate.

I am sending copies of this minute to Cabinet colleagues and to Sir Robert Armstrong.

AH Davis

for

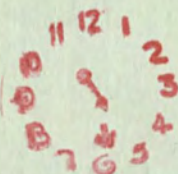
P J

18 January 1985

Approved by the Secretary of State  
and signed in his absence

nat. ind.  
Shipping  
PC

JAN 1985



18/7/84

C

CC [Signature]



Prime Minister

MO 26/3/1

DTI's minute is attached. As predicted they are opposed to the MOD line. Agree Cabinet discussion in January?

DTI will not be happy with this, and the issue may have to go back to Cabinet in January.\*

PRIME MINISTER

JR 21/12 11/12 re: navy.

Sub 19/12

TYPE 22 FRIGATES

But I agree with SNS for delivery. The damage shown

The background to the tendering exercise for two Type 22 frigates is well known to colleagues, but I set it out below for the sake of completeness.

workers in jobs through picket lines & contrivance

2. John Nott, when announcing the award of a contract for the replacement of three of the four warships lost in the Falklands campaign, indicated that there would be one more Type 22 to replace Falklands losses, for which tenders would be invited in due course. He indicated that Cammell Laird and Vosper Thornycroft would have the chance to compete for the contract for this ship: "... the fourth and final Falklands replacement will be a further Batch III Type 22 frigate. It will be ordered by competitive tender. Cammell Laird Shipbuilders Ltd and Vosper Thornycroft(UK) Ltd will be strong contenders for this order" (Hansard Vol 34, Col 130). I decided to add a second frigate to the forward programme and the competition for these two frigates was opened on 19th July 1983.

3. I set out the results, from which it is clear that Cammell Laird won the competition:

	EM (tenders for two ships)
Cammell Laird	140.0
Vosper Thornycroft	140.7
Swan Hunter	142.5

4. There then followed a re-tendering exercise because there were technical problems with each of the tenders. The results



of this exercise are below, and it is clear that Cammell Laird again won the competition:

	£M
Cammell Laird	140.0
Vosper Thornycroft	140.5
Swan Hunter	142.7

5. At the same time, the Department of Trade and Industry had been looking to the future capacity of the warshipbuilding industry, and in particular at the packaging of the industry into units most suitable to its eventual privatisation. There was a clear potential conflict between this DTI interest and the award of a contract to Cammell Laird.

6. At our discussion in Cabinet on 19th July, it was agreed that there should be a future round of tendering to include Cammell Laird. I had intended then to argue against any further delay, and to go on to recommend that we should, as is our usual practice, award the order to the winners, Cammell Laird. Much to my regret, however, a small group of militants occupied HMS EDINBURGH, being built at Cammells, and in those particular circumstances, where to award the contract might be seen to be yielding to illegal action, I did not feel able to press the point.

7. Instead I made my position on the occupation of HMS EDINBURGH, and its potential effect on the future workload at Cammell Laird, quite clear by giving an interview to Radio Merseyside in which I said:

"The people occupying one of our ships in Cammell Lairds are doing a major disservice to their community, to the prospects of the Company itself and I would want to make it clear that, as Secretary of State for Defence, I couldn't consider placing an order with a Yard that was in a position, as it patently is today, of occupying an existing contract from this Department."





In response to a question about the MOD steering orders away from Merseyside I replied:

"The way that you steer orders away from Merseyside is to occupy ships under construction. The way you get orders in Merseyside is to put in prices that are competitive and to deliver on time."

I left the workforce in no doubt that they could not expect any further orders while the occupation of HMS EDINBURGH continued. The Courts dealt with the militants, who then, with the familiar techniques of intimidation and violence, tried to stop the majority of the workers getting into the yard. They failed. Day after day the workers of Merseyside crossed the picket lines to carry on with their work on HMS EDINBURGH. In the meantime, very substantial changes in the working practices of the yard had been agreed by the newly-elected shop stewards, including the acceptance of a management-inspired programme of selective redundancy.

8. My concern at the proposal that there should be a third round of tendering arose from my conviction that it would inevitably lead to a different result, and that it would be concluded that this was the purpose of the retendering exercise. This concern proved justified when it emerged that Cammell Laird had been ordered by British Shipbuilders to tender for only one of the two ships. The excuse given for this is that in order to build two ships, Cammells would need to re-recruit men: those men who have been laid off while we have been going through these tortuous tendering exercises! From that moment on, with all their overheads loaded onto one ship, Cammells were by definition out of the competition. The results of the third round of tendering therefore indicated precisely what I warned colleagues would be the case - that Cammells should be given neither of the two orders - although it never occurred to me that so blatant a method of fixing the result would be adopted. I will have no part in it.



9. The issue I now face is what next? I must now place these long overdue orders. It appears that Swan Hunters are marginally ahead of Vosper Thornycroft on price. I have no means of knowing what Cammells' price would be for both ships, since they have been forbidden to tender. On the assumption that Swans win the contract for one frigate, the cheapest package on offer which also includes Cammells building one ship is £145.5 million. I therefore intend to place one order with Swans and the other with Cammells. I shall have to direct the Accounting Officer to place the orders in this way, since the combined cost is some £6 million more than would be the case if both orders were placed at Swans.

10. I hope that you and Cabinet colleagues can now agree to this way forward.

11. I am sending copies of this minute to other members of the Cabinet and to Sir Robert Armstrong.

Ministry of Defence  
18th December 1984



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DEPARTMENT OF TRADE AND INDUSTRY  
1-19 VICTORIA STREET  
LONDON SW1H 0ET

Telephone (Direct dialling) 01-215) 5186  
GTN 215)  
(Switchboard) 215 7877

From the Minister of State for Industry

Norman Lamont MP

The Rt Hon Peter Rees QC MP  
Chief Secretary to the Treasury  
HM Treasury  
Treasury Chambers  
Parliament Street  
LONDON SW1

17 December 1984

*Dear Chief Secretary*

**SHIPBUILDING REDUNDANCY PAYMENTS SCHEME**

*- will request if req'd*

Thank you for your letter of 11 December which concludes our joint consideration, following E(A)(84)(19th meeting), of the question of the extension of the SRPS. I am glad that you are content that the SRPS should be extended in accordance with the proposals put forward in my letter to you of 7 December. We here are content that there should be a review of DTI assistance to industry, as you suggest in your letter.

The purpose of this letter is to record, for the information of E(A) colleagues, our conclusion that the scheme should be extended for a final period of 18 months to 31 December 1986.

I propose to announce the extension, by means of a PQ and a Press Notice, on Tuesday 18 December. The Bill will be considered by Legislation Committee on Wednesday 19 December and First Reading will be on 20 December.

I am copying this letter to members of E(A) and Sir Robert Armstrong.

*Yours sincerely*

*Norman Lamont*

NORMAN LAMONT  
(Approved by the Minister and signed on his behalf)

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AF 14/12

Treasury Chambers, Parliament Street, SW1P 3AG

Norman Lamont MP  
Minister of State for Industry  
Department of Trade and Industry  
1 - 19 Victoria Street  
LONDON  
SW1H 0ET

13 December 1984

*Stan Norman*

**PROSPECT ORDERS FOR  
BRITISH SHIPBUILDERS: FERGUSON YARD**

Thank you for your letter of 5 December.  
In view of the assurances which you give I  
am now prepared to agree to the use of soft  
credit for these two orders.

*Peter Rees*

PETER REES

SHIPBUILDING: P77



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NORMAN AT 5/12

DEPARTMENT OF TRADE AND INDUSTRY  
1-19 VICTORIA STREET  
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From the Minister of State for Industry

Norman Lamont MP

**CONFIDENTIAL**

Rt Hon Peter Rees MP  
Chief Secretary  
HM Treasury  
Treasury Chambers  
Parliament Street  
LONDON SW1

5 December 1984

*De Peter*

**PROSPECTIVE ORDERS FOR BRITISH SHIPBUILDERS - FERGUSON YARD**

Thank you for your letter of 2 November.

So far as international obligations are concerned the position on the use of soft credit for export orders is essentially the same as that for home orders. We are required by the Community to observe the terms of the OECD Understanding for both export orders and home orders.

For this reason Departments have examined very carefully what defence could be advanced if the use of soft credit was discovered by the EC Commission. The letter from Patrick Jenkin to Douglas Hurd of 7 July 1982 followed a thorough review of the issue by officials. We agreed then that our main defence would be to argue that the international rules in question apply to Governments and not commercial undertakings and that British Shipbuilders like other such undertakings was free to offer its customers credit on terms which need not be constrained by the OECD Understanding.

It is true that we decided at the time that soft credit should be confined to orders from established UK owners. The reason was simply to reduce the chance of discovery. I am convinced that the risk of the Commission discovering that soft credit has been used for these two orders in question is negligible. There is no evidence of any competition from other yards. The amount of soft credit involved, 3%, is very limited; the orders themselves are pretty small in shipbuilding terms, at about £4.5m each. And it

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would be very difficult for anyone not directly concerned to deduce from the kind of information about new orders that normally becomes available in shipbuilding circles that soft credit had been involved. Finally, in the unlikely event of discovery, the defence we would use in respect of home orders - summarised above - would be equally available for the orders in question.

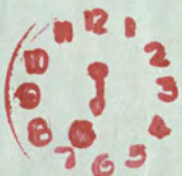
I would add that the yard concerned, Ferguson, needs these orders badly and that the prospective buyers are getting impatient and pressing hard for the deal to be concluded rapidly, failing which there is a real risk of the orders being lost.

I am copying this letter to those to whom you copied yours.

A handwritten signature in dark ink, appearing to read 'Norman Lamont', written in a cursive style.

NORMAN LAMONT

15 DEC 1984



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19/12

MR TURNBULL

4 December 1984

TYPE 22 FRIGATES

A decision should be taken soon on Type 22 Frigates. Michael Heseltine would like to give one of the two orders as a sop to Cammell Laird (CL). Partly because it is in Merseyside and partly because of the return to work committee. This makes no sense, either commercially or industrially. CL put in the highest bid; giving both orders to the lowest bidder Swan Hunter (SH) will save £6 million on a total cost of £140 million.

There are some 1,700 jobs at stake at CL. In the last month we have announced over 2,000 redundancies at SH. Both are in employment black spots. The difference is that SH men have not been out on strike whereas at CL they have been, but ultimately returned.

It would be perverse logic to reward the Birkenhead workers who only overthrew the militants once they had been taken off to gaol, at the expense of the Tyneside workers who have rejected them from the start. It could be interpreted as proving that the sit-in on HMS Edinburgh was worthwhile.

Defence competitiveness will not be helped. It will be another mouth for MOD to feed and another set of overheads to be carried. Competition will be increased - but for MOD subsidy rather than price. The way to improve procurement efficiency is to have fewer yards with more chance of being commercial and therefore more likely to compete on cost.

Worse, to share the two frigate orders between CL and SH will give each the worst of both worlds. SH will have inadequate business to make it a really viable privatisation proposition whilst CL will have one peak of work then nothing. Indeed, because the workforce could use the

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frigate as a hostage, it may make CL harder to sell rather than easier.

Commercial work is not an alternative. There is already too little of this to go round the commercial yards let alone the defence ones, and the policy is to separate the two types of work. The SH redundancies are a result of giving up commercial work.

All hope for CL is not lost. There are prospective buyers on the horizon. Failing this there are several submarines to be purchased over the next few years, one of which could go to CL who build them. [Not a good option but less bad than a T22]. Alternatively, if no buyer is found, the yard could still be linked with Vickers at Barrow that will apparently have capacity problems when the Trident programme starts.

*Peter Warry*

PETER WARRY

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~~CNO~~

Treasury Chambers, Parliament Street, SW1P 3AG

Norman Lamont MP  
Minister of State for Industry  
Department of Trade and Industry  
1 - 19 Victoria Street  
London SW1H 0ET

November 1984

**BRITISH SHIPBUILDERS - ORDER PROSPECTS  
FLEXIBILITY, AND CONTROL**

Thank you for your letter of 27 November.

I would be content for you to adopt a new system of financial control on the lines you propose. There are clear advantages in delegating decisions on individual orders as far as possible to BS, subject to proper monitoring.

As to third party guarantees, I agree that officials should continue the discussions already in hand. I also agree that officials should prepare the ground for taking decisions on the individual orders you mention if for some reason there is delay in agreeing to the proposed system.

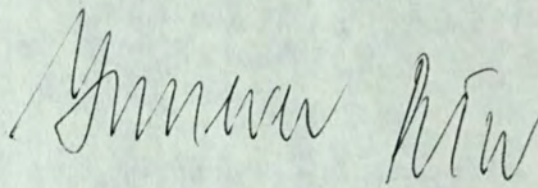
I agree with you that BS's bid for a limit of £65 million - £70 million in 1985-86 would be unacceptable. As I see it, the main purpose of the new system is to secure the rundown in capacity which Ministers collectively agreed when we discussed the BS corporate plan. An increase in the limit in 1985-86 would scarcely be compatible with that. I would be content with the figures of £55 million (with another £5 million in reserve) in 1984-85 and £45 million in 1985-86 which you propose.

There is one particular feature of your proposals which causes me difficulty, namely the idea of permitting special credit for export orders up to 4 per cent of contract price. As I said in my letter of 2 November about the prospective orders for the Ferguson Yard we have in the past set our faces against such credit for export orders. I am not clear how we could defend institutionalising it in the way you propose. Since I understand

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that you are keen to agree your new system as soon as possible, you may like to omit special credit for export orders from it to give us time to discuss more fully its justification and how it could be reconciled with our international obligations.

I am copying this letter to the Prime Minister, to Geoffrey Howe, and to Sir Robert Armstrong.

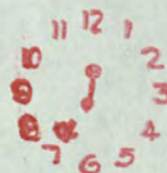


PETER REES

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30 NOV 1984



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**Conservative Research Department Brief**

## CRISIS IN THE SHIPBUILDING INDUSTRY

**Prepared For:**

Debate in the House of Commons on  
Tuesday, 27th November 1984

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## THE CRISIS IN THE SHIPBUILDING INDUSTRY

### A. Introduction

The crisis in the British shipbuilding industry is not new, but part of a continuing decline over many years. In the two years following nationalisation for example, almost seven thousand jobs were shed between July 1977 and June 1979 (BS Annual Report 1982/83). Nor has the decline in the industry been confined to this country; the problems of the world overcapacity have been felt throughout Western Europe. In the UK our share of the world market has fallen from nearly 40 per cent in 1926 to barely 2 per cent today.

When the last Labour Government introduced its Bill to nationalise the aircraft and shipbuilding industries, the then Secretary of State for Industry Mr Eric Varley noted that the prospects for shipyards throughout the world were 'bleaker than perhaps at any time in the past twenty years. The demand for new merchant ships, especially new oil tankers, has slumped to almost nothing.' (Hansard, 2nd December 1975, Col. 1460).

The situation remains acute today. Between 1977, when British shipbuilding was nationalised, and 1983 completions of world merchant ships throughout the world fell from 21.1 million compensated gross registered tonnes (cgrt) to 13.6 million (cgrt).

As Mr Varley said in 1975: .

'It is no good believing that we can go on producing what we cannot sell ... the size of the industry, like the size of any individual works, depends ultimately on the ability of the industry to sell its products in the world markets. To do that, improved efficiency and productivity are needed.' (Hansard, 2nd December 1975, Col 1448).

Such observations, although made in 1975, remains highly relevant today. They underline the approach of both the Government and British Shipbuilders in recovering a stable share of the world market for the British shipbuilding industry. Many of the decisions taken in the last two or three years have been the inevitable consequence of the necessity to adapt to a structural change in the market for marine transportation. As Mr Graham Day, Chief Executive designate of British Shipbuilders in the run up to nationalisation and now Chairman has said:

'I believe that had we taken some very difficult decisions in 1977/78 we could have got to a much lower level more quickly, and a more competitive industry would have been preserved then we have today.' (Shipbuilding News, September 1984).

The policy that would be pursued by the Labour Party, to increase subsidies without sufficient regard for world trading conditions or the need to improve quality, lower costs and quicken delivery show that they have not learned the lessons of the past.

## B. Market Environment

Despite what the General Council of British Shipping (GCBS) describe as a 'modest' fall in laid-up tonnage, prospects for world shipping are still quite gloomy. The world's large shipyards have been badly hit by the recession because their customers, the shipowners are facing a glut in capacity brought about by the drop in world trade.

In June 1980 there was only 14.7 million deadweight tonnes (mdwt) of idle merchant shipping around the world. By June 1983 this had risen to a peak of 100.3 mdwt. Since then there has been a gradual fall in laid-up shipping to 65.9 mdwt by August 1984.

In April 1984 there were 1,566 ships or 11 per cent of the world tonnage laid up. The Annual Report of Lloyd's Register for 1983 reported that for the first time since the Second World War there had been a decline in the world fleet. This has been reflected in the decline in the work completed by shipbuilding yards around the world. (See Section A).

## C. Recent Developments in British Shipbuilding

### 1. Finances (see also Appendix)

The original External Financing Limit (EFL) for 1983-84 of £158 million was reset at a record £268 million; of the increase £88 million was to cover the costs of the disposal of Scott-Lithgow and a further £22 million was to meet the effects of the continuing world recession in merchant shipbuilding.

Due to the impending privatisation of warshipbuilding and the reorganisation of the Corporation into two divisions (See 3 below), the Government has set a separate limit for each new division in 1984/85. The total limit will be £217 million; £80 million for warshipbuilding and £137 million for the rest of the Corporation.

In June 1984 the Government raised the Corporation's borrowing limit from £1,000 million to £1,100 million. As Mr Norman Lamont, noted at the time: 'the order provides scope for substantial increases in support for British Shipbuilders.' (Hansard, 27th June 1984, Col 1093).

In 1983/84 the Corporation made a trading loss of £161 million of which £75 million was contributed by Scott-Lithgow, which is now in the private sector, following a successful rescue plan in March. These losses compare with £117 million in 1982/83.

### 2. Employment and Closures

BS's work force has been reduced from 87,500 at nationalisation in 1977 to 48,550 by the end of March 1984. In the course of 1983/84 9,442 were shed as part of the Corporation's survival plan, almost all voluntarily. A further 4,000 jobs have moved to the private sector (See Section E). A number of yards were closed in January as part of the continuing nationalisation of the Corporation's activities; there were Henry Robb at Leith (383 jobs) - none of these yards had had any work since Christmas. Because of the lack of work at

Cammell Laird, over 1,000 men have been made redundant in 1984/85. At 31st March 1984 14,400 were engaged in merchant ship and engine building, 1,900 in offshore rig construction, 1,100 in shiprepair, 4,900 in engineering and 25,700 in warship building.

Further redundancies were announced on 21st November 1984. Swan Hunter, the composite yard on the Tyne will lose 2,100 jobs and Vosper Thornycroft is to shed 790 jobs. These were due to a lack of orders and where possible the reductions will be achieved on a voluntary basis. In all cases generous redundancy terms are available. (See Section F).

### 3. Reorganisation

In March 1984 British Shipbuilders announced major changes in organisation as part of its attempt to curb heavy losses and win much needed orders. The Corporation will operate with only two divisions instead of five. Since April there has been a division combining merchant and composite yards.

In addition there has been a cut back at the Newcastle-upon-Tyne headquarters by 20 per cent; the savings of £1.5 million will be reallocated to product development.

### 4. Orders

In recent years there has been a pattern of declining areas. In 1983/84 new orders amounted to only 117,000 cgrt. This figure was substantially below the figure of 179,000 cgrt registered in 1982/83.

Mr Graham Day outlined the reasons for this poor performance:

'Obviously the market was very tight, and there has not been any movement upwards on average over the past five years; our competitiveness was declining; our costs were increasing and our delivery on time record was worsening. Finally we had not shifted our strategy progressively to respond to the different element in the market.' (Shipbuilding News, September 1984)

The target for orders this year is around 200,000 cgrt, or 40 per cent up on last year. In the first quarter of the year orders for 70,000 cgrt had been achieved, indicating that the target will be reached.

When Graham Day took office last year there were 25 pieces of business under discussion, now there are 100. As he has said,

'If ... we needed 10 ships to meet our target we would have needed a 40 per cent success rate when there were only 25 bits of business under discussion. With 100 pieces of business under discussion we need a success rate of 10 per cent. Our chances of success are therefore much greater.' (Shipbuilding News, November 1984)

### 5. Individual Yards

The record of individual yards has been mixed. On the credit side Sunderland



Shipbuilders have a much improved record with their last 15 ships completed on time. The men worked through their annual holiday in July to launch the Mexican container ship 'Colima' on time. Govan has a consistent record on delivery and improved competitiveness. A valuable £30 million order for Jebsens was recently completed on time. In March an order from the CEGB was won for 3 colliers, worth £28 million. Ferguson-Ailsa was recently reported to be close to winning a £13 million Canadian order that would safeguard employment at its two yards. Following the completion of work on the Ark Royal and the Atlantic Conveyor, Swan Hunter is currently carrying out work on the two navy frigates. An order worth £40 million was recently won against fierce competition for the replacement of the Sir Galahad. It will employ 700 people up until early 1987.

The other side of this picture has been Cammell Laird on Merseyside where a sit in by around 130 of the workforce brought work on a British Gas rig and a Type 42 destroyer to a halt. This action by a minority group guaranteed that the yard would not win a £125 million order from Sun Oil. This type of action can only harm the reputation of a yard and a majority of its workforce that had, until recently, a consistently good record.

#### D. The Corporate Plan

The Corporation's strategy for dealing with the present adverse trading conditions are contained in their corporate plan for the period 1984-85 to 1987-88 which was placed before the House on 25th July 1984.

In the light of the Government's plans to privatise the warship and composite yards (See Section E) the Corporation's primary objective will be to concentrate its resources on a stable, cost effective mainstream merchant shipbuilding business.

In a statement to the House on British Shipbuilders' future Mr Norman Tebbit outlined the challenge facing the Corporation:

'the key to its future depends on improving the efficiency of production of merchant ships. It sees the primary need as being to increase flexibility and productivity. In all this a further key element will be the implementation of the flexible working practices agreed with the workforce earlier this year.' (Hansard, 25th July 1984, Col 998).

The main points of the Plan are:

- The Corporation will in future concentrate on six merchant ship yards. These will be Appledore, Ferguson Ailsa, Austin and Pickersgill, Smith's Dock, Sunderland Shipbuilders and Govan Shipbuilders.
- These 6 yards will employ around 9,600 backed by a reduced engine building facility employing 1,300 at its two yards at Greenock and Wallsend.
- No further yard closures are envisaged up to 1988 and there will be near constant employment levels.
- A drop in world market share, from 2 or 3 per cent to 1.5 per cent is expected, representing an order book in the range of 180,000 to 210,000

cgrt. This is at a considerably higher level than the orders won in 1983/84.

- A capacity to erect and test slow speed diesel engines is considered strategically important and will be maintained.
- An improved marketing strategy is being developed to reduce direct competition with Far East price leaders and aims for increased value added areas of the market such as diving support vessels and dredgers. The central marketing department has recently been restructured with three regional directorates with specific global areas of coverage.

#### E. Privatisation

The Government is committed to the promotion of private ownership in the shipbuilding industry. The British Shipbuilders Act 1983 enables the Secretary of State for Trade and Industry to direct British Shipbuilders to dispose of particular assets or subsidiaries. A number of disposals have taken place already; Scott-Lithgow was saved from closure protecting around 2,000 jobs and as the Financial Times has said it 'is coming back from the dead'. (FT 22nd September 1984). Redheads, the Tyneside shiprepair yard bought by its workforce of 80, now has an annual turnover of £2 million; Tyne Shiprepair Ltd and Grangemouth Dockyards Ltd were the subject of management buy-outs which preserved 600 jobs. By March 1984 the former had booked work for 27 ships worth around £3 million, just 4 weeks after it became a private company.

The Government recently announced plans to dispose of the Warship and composite yards; Vickers in Barrow, Yarrow on the Clyde, Vosper Thornycroft at Southampton, Hall Russell at Aberdeen, Brooke Marine at Lowestoft, Swan Hunter on Tyneside and Cammell Laird at Birkenhead. Mr Norman Tebbit said

'I have today asked the corporation ... to dispose of those parts of the corporation engaged mainly or wholly in warship building. To secure the maximum practical extent of fair competition we would prefer to see the yards sold separately or in small groups - I have ... also asked the Corporation to set in hand contingency preparations for a flotation on the Stock Exchange of all or some of the companies in case individual sales may not be achieved. I believe that this will enable the Corporation to pursue single mindedly its aims for its merchant shipbuilding business and to take the steps to improve efficiency on which its long term future depends, while providing an assured competitive warship building capability.' (Hansard, 25th July 1984, Col 999).

He also indicated his support for buy-outs by management and workforce so long as these were commercial offers.

32 warships are currently being built and the total value of these 32 orders is £2,800 million. Over the next decade the Royal Navy will be ordering 12 of the new Type 23 frigates at cost of approximately £100 million.

#### F. Government Support

The Government's support for the industry takes different forms. Like all nationalised industries, British shipbuilders look to the Treasury for external finance which it usually receives in the form of loans and public dividend capital. Total support for BS has amounted to £1,170 million since 1979 broken down as follows:

£844 million in public dividend capital  
£203 million from the intervention fund  
£123 million in special redundancy payments

The subsidy element in the financing in the Corporation's losses last year is thought to amount to £18,000 per worker in the merchant division.

The Intervention Fund exists to help BS compete with cheap Far Eastern prices. The previous tranche of the UK Intervention Fund, at a rate of 15 per cent of total contract price, expired in June 1984. The most notable example of its use was the provision of £10 million by the Government to ensure that Cunard built the replacement for the Atlantic Conveyor at Swan Hunter instead of Hyundai in Korea. The Government is currently discussing with the European Commission the possibility of a new regime for the UK industry for the period 1984/85 and 1985/86. This would involve an increase in the level of assistance of up to 35 per cent of contract price. Mr Norman Lamont has said:

'We are well aware that the cost/price gap faced by BS, as with all Western European shipbuilders who are generally competing with the Far East, is growing. We have therefore notified the European Commission of our intention to increase the level of price support we offer under the Intervention Fund. We, and increasingly our European partners, believe that the present arrangements are no longer sufficient to secure an adequate workload for the United Kingdom.' (Hansard, 27th June 1984, Col 1097)

The Shipbuilding Redundancy Payment Scheme was introduced in 1978 to assist in the restructuring of the industry. The Conservative Government has subsequently extended the assistance available to December 1986. The scheme provides for lump sum payments to all who are made redundant and weekly support benefit for up to two years to those over 40, depending on their new employment, if any.

On typical earnings of £120 per week, the lump sum payable to an employee with twenty years service would range from £5,050 at age 35 to £5,800 at age 56 and over. Weekly support benefits to those over 40 would be £46 per week whilst they remain unemployed. Since 1977 around 35,000 redundant workers have benefitted under the scheme at a cost of more than £130 million. Around 7,000 individuals are currently in receipt of weekly benefits.

#### G. World Comparisons

The Shipbuilding industry has been faced with severe difficulties throughout the world, not just the UK. Competition in world markets is severe at a time when world shipbuilding capacity is reckoned to be 40 per cent greater than is required. Some estimates have suggested that Far Eastern prices are at least 30 per cent below those in Europe.

Japan. The total order book increased to 14 million gross tonnes which accounts for over 40 per cent of the world order book. However, this follows a fall of 35 per cent in 1982 of world forward orders over 1981. The shipbuilding division of the large Hitachi Zosen combine reported that their 6 yards were working at barely 60 per cent capacity (Sunday Times, 11th March 1984).

South Korea. The South Korean industry is now second only to Japan. In 1974 it ranked only 70th in the world. Last year it increased its share of the world order book from 9 per cent to 14 per cent. It is often blamed by its western competitors for unfair competition. The Seoul Government is accused of granting excessive subsidies and export credit to enable its yards to quote prices up to 35 per cent cheaper than its European rivals. The Koreans however claim that their two largest yards, Daewoo and Hyundai, receive no direct Government subsidy - though they did benefit from an initial 5 year export credit, but the terms are said to be less favourable than the Japanese offer. Korean yards say they are cheaper because their yards are more modern and efficient, because their raw materials, particularly steel, are cheaper than in Europe, and because they have a cheap and disciplined workforce. The average working week in Korean ship yards is 60 hours and wages are about one third of those paid in Japan. There is no doubt that their continued expansion is not only unhelpful to the present world overcapacity, but it will also harm their own prospects in the long run.

Sweden. In 1975 its yards employed 28,000 people building ships. By 1983 the figure was under 8,000. The Kockums yard is an example where severe restructuring has turned consistent loss-making into a small profit in 1982. The Annual Report of Lloyds Register for 1983 noted that 'Following dramatic adjustments to Swedish shipbuilding capacity in recent years the future looks more encouraging'

West Germany. New orders received in 1983 dropped from 4.4 per cent of the world's new orders to 2.4 per cent. HDW has been forced to close its merchant ship building in Hamburg, while A G Weser, part of the Krupp Group has closed its large yard in Bremen with a loss of 2,000 jobs. (Financial Times, 14th March 1984).

France. Their order book fell by 31 per cent in 1983. A plan to reduce capacity by 30 per cent over three years was announced earlier this year involving the loss of 5,000 jobs out of an industry employing 22,000.

Spain. Under a new restructuring plan two of Spain's five big yards will close. This will mean the loss of 17,000 jobs from a total workforce currently at 40,000. (Shipbuilding News, November 1984).

VOLUME OF SHIPBUILDING WORK

(m gross registered tons)

	Completions			End-year order total		
	1973	1982	1983	1973	1982	1983
Japan	14.7	6.7	6.7	59.6	10.1	14.0
S Korea	0.01	1.4	1.5	1.3	2.6	4.6
W Europe	12.0	3.8	4.1	54.9	7.7	5.7
inc Sweden	2.3	0.3	0.3	10.7	0.6	0.5
W Germany	1.9	0.6	0.8	7.3	0.9	0.6
UK	1.1	0.4	0.5	7.5	1.0	0.6
Spain	1.3	0.6	0.5	7.2	1.5	1.2
France	1.2	0.3	0.3	5.2	0.7	0.5
World Total	30.4	16.7	15.7	128.9	29.2	32.6

Source: Lloyd's Register of Shipping - quoted in Financial Times 16th March 1984

## APPENDIX

### BRIEF 1: CORPORATE PERFORMANCE AND GOVERNMENT SUPPORT

KEY DATA

PERFORMANCE (£M)	77/78	78/79	79/80	80/81	81/82	82/83	83/84	1984/5 (year to date)
Profit(Loss)	-104	-50	-110	-41	-20	-117	-151	N/A
<hr/>								
External Finance Limit	-	83	250	185	150	122	158*	217
Requirement	95	79	189	170	146	120	306	N/A
<hr/>								
Capital Expenditure	20	27	18	17	37	43	48	not set
<hr/>								
GOVERNMENT SUPPORT (£M)								
NLF & POC	-	55	181	110	107	76	281	89
Intervention Fund Receipts	27	11	31	40	46	44	33	9
SRPS	-	5	16	20	14	16	35	22
<hr/>								
CUMULATIVE TOTAL SUPPORT SINCE 1979			228	398	565	701	1050	1170
<hr/>								
Home credit	For ships - 80% of contract price at 7.5% over 8 1/2 years (OECD)							
	Offshore - 85% of contract price at 12.5% over 5 years (Consensus)							
<hr/>								
EMPLOYMENT								
<hr/>								
Number employed '000	85	80	70	68	66	63	49	46
Total Job Losses '000	0	5	15	17	19	22	36	39
<hr/>								



From the Minister of State for Industry

NAPM AS 27/11  
DEPARTMENT OF TRADE AND INDUSTRY  
1-19 VICTORIA STREET  
LONDON SW1H 0ET

Telephone (Direct dialling) 01-215-

GTN 215

(Switchboard) 215 7877

5186

Norman Lamont MP

**CONFIDENTIAL**

The Rt Hon Peter Rees QC MP  
Chief Secretary  
HM Treasury  
Treasury Chambers  
Parliament Street  
LONDON SW1

27 November 1984

**BRITISH SHIPBUILDERS - ORDER PROSPECTS, FLEXIBILITY AND CONTROL**

When E(A) discussed British Shipbuilders Corporate Plan at E(A)(84) 19th Meeting, Norman Tebbit said that he was examining the possibility of requiring BS to manage for themselves a total provision to cover IF and soft credit, subject to appropriate ground rules.

My officials have been discussing this further with yours and I am now writing to ask for your agreement to the system of improved financial control by setting a limit on contract support and increased flexibility for BS described in the paper at Annex A, recognising that the detailed provisions on IF and soft credit cannot be finalised until we know the outcome of the negotiations in Brussels of our application for a new tranche of IF. Once the system is in place we would not need to approve individual orders which complied with the rules. This, coupled with the improved financial control, will give BS the responsibility for deciding how best to use the sums available while distancing the Government from the decisions which affect the future of individual yards.

Meanwhile, Graham Day has come to me about the situation in the main merchant yards particularly in the North East which are rapidly running out of work, and where he fears that unless orders can be placed very quickly, there could be industrial relations problems which could spread to the yards affected by privatisation in a way which would damage our privatisation programme. He has accordingly looked for a package of orders (details of which have been passed to your officials) which if secured could very rapidly provide work to fill the gap in the yards concerned.

1MOAIY



I want to use BS's need to secure these orders as a means of getting their agreement to the system proposed and to the limits for both 1984/5 and 1985/6. There are two main outstanding problems.

- The package of orders Graham Day has identified would require BS to give a number of third party financial guarantees. We need to devise appropriate rules both to determine the conditions under which BS give such guarantees and how they should be valued against the limit on contract support. I have accordingly asked my officials to discuss with yours how to do this.
- The limit of contract support to be set for 1984/5.

We have not so far been able to agree limits with BS. This is partly because Graham Day is abroad until the end of the month and partly because we have deliberately avoided setting BS a capacity target. They are asking for £55m-£60m in 1984/5 and for £65m-£70m in 1985/6. I regard the latter as completely unacceptable. I therefore propose to offer BS a limit of £55m in 1984/5 and £45m in 1985/6 (these are compatible with E(A)'s decisions on the Corporate Plan) and, exceptionally, to allow greater year-end flexibility to enable BS to take orders which they had hoped to take in 1984/5 in the first three months of 1985/6 to ensure that they do fill their current workload gap quickly. In addition, since I believe BS can mount good arguments in favour of £60m contract support as being compatible with the 200,000 cgrt order intake which we are prepared to contemplate for 1984/5, I would propose to hold in reserve for use if necessary in my discussions with them a further £5m for use in 1984/5 which would not be available for carrying forward into 1985/6.

Even so, we may well have a row with BS over the figures, but these are the most that are compatible with our decision on the Corporate Plan. If there is a row, I believe we can defend our position.

Once the arrangements are in place we shall no longer need to be involved in decisions on individual orders except those which fail to meet the criteria laid down for cases in which BS can use their own discretion. I hope there will be very few exceptions.

I should however mention one particular order prospect, for the Ailsa yard. It concerns two £2.5m vessels for Seaforth Maritime - a UK company - and involves a special credit element of 2.8% of contract price on top of Intervention Fund at 15%, shipbuilders' relief at 2% plus standard credit support. When deciding on BS's Corporate Plan earlier this year we regarded Ailsa as a candidate





for early disposal or closure. This order would prolong its life by some eight months, until November 1985. Nevertheless, I propose to agree to the order being taken on those terms, provided the usual assessment of costings etc is satisfactory. Any Government support will come out of their total provision for the current year. The subsidies involved are tolerable and to object would cut across the approach we agreed of standing back and allowing BS to decide how best to allocate funds available for contract support within the limits to be set.

I very much hope that we can get the system in place in time to allow BS to conclude a package of orders in the near future to fill their order gap. However, if there is delay in agreeing to our proposed system, decisions might be needed on at least some of these orders before the new arrangements for controlling contract support are in place. To prepare for this eventuality I suggest that our officials get together to prepare the ground in case quick decisions are needed.

Paragraph 27 of our paper at Annex A sets out the ground rules on the flexibility BS would have in deciding on subsidy levels for particular orders without prior reference to the Department. These rules are designed to ensure, as far as possible, that the terms on which orders are taken comply with international rules and to minimise the risk of discovery in cases where these rules are not fully observed. In particular we are proposing limits on the allowable amount of special credit of 8% of contract price for UK owners and 4% for export orders.

These arrangements modify the approach agreed inter-Departmentally in 1982 and recorded in Patrick Jenkin's letter of 7 July of that year to Douglas Hurd. I am convinced, however, that the proposed criteria would ensure that the chances of running into problems with the EC Commission were low enough to be acceptable.

I would welcome your agreement to these proposals by 4 December.

I am copying this letter to the Prime Minister, the Foreign Secretary and Sir Robert Armstrong.

*NORMAN LAMONT*  
NORMAN LAMONT

1MOAIY



FINANCIAL CONTROL AND FLEXIBILITY FOR BRITISH SHIPBUILDERS  
MERCHANT SHIPBUILDING OPERATIONS

INTRODUCTION

The only financial constraints at present placed upon BS are the two EFLS.

2 Historically, with the exception of Scott Lithgow, BS has a good record of staying within its EFL. Revisions of EFL have proved necessary in only two of the seven years since nationalisation.

3 Up to 1983/4, the EFL was supplemented by an overt loss target. From 1978/9 to 1981/2 they usually met their loss targets, sometimes undershooting. However in 1982/3 BS sustained a loss of £117m against a limit of £10m. Given this clear failure of the control, and increasing EC objections to our condoning loss financing by setting such a limit, for 1983/4 we set only an informal target of £20 million. The outturn was £161 million, including the provisional costs of Scott Lithgow. The loss limits have not proved an effective control for two main reasons. First it is clearly much more difficult to control trading loss in the present phase of radical restructuring. Second there is no incentive to BS to stick to the limits; they suffer no financial or other penalty if they fail to do so.

4 Simultaneously the structure and operation of the present subsidy arrangements has placed constraints on BS' commercial freedom of action. BS argue that the need for detailed vetting of each IF application and Ministerial clearance of these and of any special elements of financial packages has presented BS with very considerable practical problems in contract negotiations. Most recently the public knowledge that the UK has sought - but not yet achieved - EC approval for increasing levels of aid has introduced further uncertainty into the market.

5 The purpose of this paper is to outline proposals for a new financial control and contract approval system accompanied by the devolution of construction of financial packages to BS. It consists of three parts:

- I - Framework for a new system
- II - Structural details
- III - Proposed guidelines and constraints

I - FRAMEWORK FOR NEW SYSTEM

6 A primary aim of any new system - supplementary to the EFL controls - should be to reduce the risk of BS making losses greater than the Government is prepared to finance. The objective is to place a strict limit, insofar as this is possible, on HMG's exposure to excessive losses by limiting BS's



ability to take new loss-making work and to do so in a way which leaves BS with the main responsibility for deciding what work to take. A system which operates on the aggregate cost of orders would reduce the risk of future losses, while allowing BS to take more orders within the same overall cost if they become more efficient.

7 The aggregate cost of orders (the price-cost gap) is met in three ways:

- IF credit
- Special credit )
- Contract losses)
- under S7 and S8 of the Industrial Development Act 1982
- both funded by PDC

The control system will apply to all three, by setting an annual limit on the aggregate cost of IF credit, special credit and contract losses on all orders. In addition any third party financial guarantees given by BS will be valued and that valuation will count against the limit.

8 Intervention Fund credited will be the main component. The maximum volume and rate need to be consistent with the outcome of the negotiations in Brussels. An annual limit will set the amount of IF available to be credited against new orders.

9 Special Credit Terms offered by BS are at present subject to ad hoc Ministerial assent BS will be free to offer special credit provided that the cost falls within the aggregate limit and subject to general guidelines (see para 27 below) as to the maximum levels on individual contract. Special credit is recorded by BS within contract loss (see para 10 below).

10 Contract Losses are recorded in the monthly management accounts as well as in the annual accounts. BS reassess contract loss forecasts for the whole contract at least every three months. The auditors keep an eye on their forecasting, especially at the year end. Although we expect BS to seek to cover as far as possible the anticipated price-cost gap with IF and special credit, no separate constraint on maximum losses will be set provided that they do not cause the aggregate new order cost limit to be exceeded.

## II - STRUCTURAL DETAILS

11 The system will thus consist of a predetermined annual limit for the funds available for commitment in the form of:

- IF
- contract losses, including soft credit.

This limit would apply to all work taken by Austin and Pickersgill, Govan, Smiths Dock, Sunderland, Ferguson/Ailsa and Appledore, and to any merchant work taken by other yards while they remain in the Corporation.



12 As new commitments appear, either as a result of new contracts or by an increase in the management account estimates of the loss on existing contracts, they are deducted from the funds available. When the limit is exhausted or seems likely to be exhausted no further commitments can be made which would cause the limit to be exceeded.

#### Intervention Fund

13 For a given new order, the whole of the IF committed is to be scored against the limit for the year in which the order was taken (see paragraph 17 below for discussion of order dates).

#### Contract Losses

14 Contract losses on actual contracts, excluding yard under-recoveries but including Corporate contract contingencies, are to be scored for the whole contract as soon as they appear in the management accounts, either as new provisions for new contracts or as alterations in loss provisions for older contracts.

15 The Department will need advance notification of any changes in BS accounting practice in respect of overhead allocation and recovery.

#### Special Credit (provided by BS)

16 Special credit is recorded in the BS management accounts as a contract loss. There is therefore no need for provision for scoring it separately, though the DTI will wish to keep some check on terms involved.

#### Date of Order

17 The date at which an order is taken is defined variously for various purposes. For the purposes of this control system, it could be the date of signature of the Building contract.

#### Year end Flexibility

18 The system will have a limited amount of flexibility in order to reduce problems at the year end. For example, without flexibility BS might go for an order expecting to get it in year 1, having left sufficient headroom in that limit, only to find that the contract was not signed until after April 1. Without flexibility BS would have to score it in year 2, leaving an underspend in year 1. Equally an order might come to fruition earlier than expected and have to be held back until the new financial year, and possibly lost, as a result.



19 The following provisions for year end flexibility will apply:

(a) BS should be permitted to apply unspent year 1 funds, up to a limit of 25% of the year 1 total, to orders taken in the first 3 months of year 2. Equally year 2 funds, up to 25% of the year 2 total, could be applied to orders taken in March of year 1.

(b) in addition, year 2 funds, up to 25% of the year 2 total, could be applied to orders taken at any point in year 1, but provided that the ships will not start building until year 2 or later.

(c) if, after making full use of these flexibility provisions, it appears at the time of the annual audit, or earlier, that BS have overshoot the year 1 control limit, then that overshoot will be deducted from the year 2 limit.

#### Financial Guarantees

20 [The conditions under which the Corporation gives third party guarantees and the valuation of such guarantees for scoring against the limit is currently under discussion between officials.]

#### Exceptional Items

21 Experience shows that BS will suffer some large losses, such as owner defaults. It could be onerous if these were all to be directly scored against the limit regardless of circumstances - one default could absorb a substantial part of the annual limit. These should therefore be treated ad hoc as they arise.

#### Information Requirements

22 For DTI control purpose we would need to know for each order taken at least:

- IF committed
- special credit and any other contract loss
- the headroom available within the limit, after deducting other commitments and contracts losses according to the rules above
- a description of the full financial arrangements.

23 Our detailed requirements would be set out in a standard form for completion by BS.



### III - PROPOSED GUIDELINES AND CONSTRAINTS

24 The principal constraint is of course the overall annual limit. Analysis of BS performance in terms of loss (including IF) per cgrt during 1983/4 on orders completed or in hand at the end 1983/4 suggests that, after taking account of Corporate Plan productivity targets, the 1984/5 limit should be set at [£50m]. This will cover IF commitments and loss provisions taken in that year plus increases or decreases in 1984/5 of loss provisions on earlier contracts. For 1985/6 the limit should be reduced, to reflect expected productivity improvements, to [£40m].

25 Within this overall constraint BS will either no longer be required to clear with the Department beforehand and in detail the IF and any other subsidies involved for an order which meets certain conditions outlined in paragraph 27 below, or formal clearance will be available immediately on receipt of the necessary information. The IF scheme will otherwise be operated as at present, with full post hoc evaluation of outturn costs and appropriate clawback arrangements for overpayment of grant.

26 BS will no longer be required to produce detailed cost estimates in each case to demonstrate that orders were not taken at a loss. Whether BS will continue to be required to certify to this effect will depend on EC considerations. Such losses as are incurred on individual contracts will be deducted from the available funds under the proposed new financial control arrangements.

27 In order to meet EC requirements it will be necessary to set certain conditions which orders qualifying for the more flexible arrangements would have to meet. The proposed conditions are as follows:

(i) IF intensity to be within the limit agreed with the EC Commission. Cumulative IF volume applied not to exceed tranche agreed with EC.

(ii) [No orders to be taken on terms manifestly involving a loss ab initio after crediting IF and any special credit]

(iii) A limit of 8% of contract price in NPV terms on the amount of special credit that can be applied to individual contracts from UK shipowners and 4% for export orders.

(iv) BS must consult the Department in advance about the terms of any IF or special credit in all cases where there is competition from the UK private sector or from Harland Wolff, and in all cases where the only competition comes from within the EC.



28 Financial arrangements not meeting these conditions would require Government clearance in advance of those aspects falling outside the guidelines.

DEPARTMENT OF TRADE & INDUSTRY  
19 NOVEMBER 1984

## MERCHANT YARDS CURRENT AND FUTURE EMPLOYMENT

YARD	TOTAL NUMBER EMPLOYED  AT SEPT 84	NUMBERS CURRENTLY LAID OFF		NUMBERS LAID OFF/ REDUNDANT		NUMBERS LAID OFF/ REDUNDANT	
		NOVEMBER		JANUARY		APRIL	
		STEEL	OUTFIT	STEEL	OUTFIT	STEEL	OUTFIT
A & P	1833	550	-	400	70	720	405
GOVAN	2201	60	190	45	55	600	80
SMITHS DOCK	1518	-	-	110	66	280	70
SUNDERLAND	2052	-	150*	-	50*	315	40
FERGUSON (PT GLASGOW)	396	-	-	30	-	-	15
- AILSA (TROON)	383	60	80	60	47	-	47

Note \* the outfit surplus is being absorbed by the Steelwork overload under Phase V



Shipbuilding Pt 7

27 NOV 1964

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12/11  
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DEPARTMENT OF TRADE AND INDUSTRY  
1-19 VICTORIA STREET  
LONDON SW1H 0ET 5422  
TELEPHONE DIRECT LINE 01-215  
SWITCHBOARD 01-215 7877

PS/  
Secretary of State for Trade and Industry

16 November 1984

Andrew Turnbull Esq  
Private Secretary to the  
Prime Minister  
10 Downing Street  
London SW1

*Dear Andrew,*

**BRITISH SHIPBUILDERS: DISPOSAL OF BROOKE MARINE**

In your letter of 15 October you recorded the Prime Minister's concern about the possible reaction of the Omani Government if their acquisition of a stake in Brooke Marine led to any industrial trouble there and asked whether there were any precedents.

2 British Shipbuilders had indeed considered this possibility. There are no precedents to guide either BS or the Government but BS believe that an announcement that the Omanis had purchased a minority stake in Brooke Marine could give some further ammunition to those seeking to frustrate privatisation. Nonetheless, BS think that this factor is in itself not sufficiently significant to trigger any serious industrial relations problems.

3 The nearest direct equivalent is probably those cases where Ministers, including the Prime Minister, send messages of support for export business to the Governments. Such messages are always drafted to ensure that if the Government does lend support to export business, there is no recourse to the Government for failure to perform the contract satisfactorily. We do not propose an analogous message in this case. But it would seem right to take care that nothing is said either by the Government or by British Shipbuilders in connection with the future performance of Brooke Marine which would lead to recourse to the Government. We are advising BS accordingly.

4 I am copying this letter to Richard Broadbent (Chief Secretary's Office), Peter Ricketts (FCO), Richard Mottram (MoD) and Richard Hatfield (Cabinet Office).

*Yours ever,*

M C MCCARTHY  
Private Secretary

JH1BMA

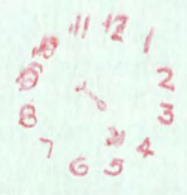
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Not Incl: Shipbuilding: Pt 7

DEPARTMENT OF TRADE AND INDUSTRY  
4th FLOOR  
LONDON SW1W 0HQ  
TELEPHONE: 01-275 3100  
FACSIMILE: 01-275 3101



19 NOV 1984



*[Faint handwritten notes or signatures]*



Treasury Chambers, Parliament Street, SW1P 3AG

Norman Lamont Esq MP  
Minister of State  
Department of Trade and Industry  
1 - 19 Victoria Street  
London SW1H 0ET

2 November 1984

*Dear Minister,*

**PROSPECTIVE ORDERS FOR BRITISH SHIPBUILDERS  
FERGUSON YARD**

Thank you for your letter of 25 September about the prospective orders for the Ferguson yard for which you seek agreement to an interest make-up arrangement for a non-UK owner.

2 As you know, we have in the past set our face against such arrangements for export orders which, I am advised, are clearly contrary to the spirit of our OECD obligations and may even be contrary to the letter of them. In the light of this, I should have been much happier if the extra subsidy could have been applied by way of price reduction. I gather, however, that this presents difficulties to BS. Before I can consider the credit routes I should be grateful to know how you would reconcile our agreement to these arrangements with our OECD obligations.

3 Copies of this letter go to other E(A) colleagues, Geoffrey Howe, Douglas Hurd, and Sir Robert Armstrong.

*Yours Sincerely,*

*Peter Rees*

PETER REES

*(Approved by the Chief Secretary  
and signed in his  
absence)*

Shipbuilding Policy: NAT. IND. Pt 7.

2 NOV 1984



Prime Minister

Did this come up? If so, were you able to visit the Liverpool Lobby?

CONFIDENTIAL

AT 29/10

It came up - I mention

MR TURNBULL

29 October 1984 Commitment

CAMELL LAIRD

merely asking which other yard they intended to

I understand that Patrick Jenkin is to lunch with the Prime Minister today and intends to raise the issue of placing one of the two Type 22 Frigate orders at Cammell Laird.

close put

The Cammell Laird sit-in has only recently been broken and the vast bulk of the workforce have disowned the militants. The official union line is more confused. Cammell Laird is likely to run out of work around the end of the year. The refit of the submarine HMS Otter has now been awarded to a private sector shiprepairer, Humber Graving Dock; and there is now little potential work other than the T22 frigates.

The Vosper Thornycroft and Swan Hunter yards of British Shipbuilders also bid for the frigate orders. Swan Hunter was cheapest at £73.5 million and Cammell Laird the most expensive at £75.4 million (it only bid for one), with Vospers falling in between.

Vospers is just about saleable without the frigate orders, but Swan Hunter where 2,000 people are to be made redundant and the number of yards there slimmed from four to two, is unlikely to be saleable without the substantial new orders that these frigates would represent.

Although both Cammell Laird and Swan Hunter have been making substantial losses, Swan Hunter with the receipt of both orders could become a genuinely commercial proposition, particularly with the slimming down of the workforce. Giving one of the frigate orders to Cammell Laird would not make it any easier to sell Cammell Laird but would make it significantly more difficult to sell Swan Hunter.

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Our view, and also that of British Shipbuilders and DTI officials, is that the only sensible course is to give both T22 orders to Swan Hunter, who in any event have made the lowest bid, and to recognise that Cammell Laird can only be sold as a redundant yard at best.

*Peter Warry*

PETER WARRY

CONFIDENTIAL

CONFIDENTIAL

*file* MFJAGH



10 DOWNING STREET

*From the Private Secretary*

15 October 1984

*Dear Ruth,*

British Shipbuilders: Disposal of Brooke Marine

*B171*  
The Prime Minister has seen your letter to me of 20 September and comments from the Foreign Secretary, Secretary of State for Defence and Chief Secretary. She agrees that the Omani Government should be allowed to acquire a minority stake in Brooke Marine. She has expressed concern however that if there is industrial trouble there the Omani Government might misunderstand it and the Government's good faith might somehow be queried. She has asked whether there are any precedents which are relevant.

I am copying this letter to Richard Broadbent (Chief Secretary's Office), Peter Ricketts (Foreign and Commonwealth Office), Richard Mottram (Ministry of Defence) and Richard Hatfield (Cabinet Office).

*Yours sincerely*  
*Andrew Turnbull*

Andrew Turnbull

Miss Ruth Thompson  
Department of Trade and Industry.

CONFIDENTIAL

*SS*





ml

10 DOWNING STREET

From the Private Secretary

Prime Minister ①

BS are ready to sell Brooke Mansel  
Lowestoft and seek advice on how to  
respond to Omani interest. DTI  
suggest that sale of minority stake to  
be Omani Government would be acceptable  
but not an outright sale of majority control.  
Other Departments endorse this

Agree?

AT

10/10

I agree - but I feel  
unhappy about it - if

we get industrial  
trouble there - our

Omani friends might not  
understand it - and our good  
faith might somehow be ruined

Are there any precedents?



MINISTRY OF DEFENCE  
 MAIN BUILDING WHITEHALL LONDON SW1  
 Telephone 01-~~8307822~~ 218 2111/3

MO 26/3/3

9th October 1984

*Dear Andrew*

BRITISH SHIPBUILDERS: DISPOSAL OF BROOKE MARINE

*with AT* The Defence Secretary has seen Ruth Thompson's letter to you of 20th September about the Omani interest in taking a large majority stake in Brooke Marine or even in buying the yard outright.

Mr Heseltine agrees that there appear to be no security or defence objections, to suitable foreign control of Brooke Marine. The yard is not one on which the Ministry of Defence is dependent to any significant degree, although it recently received an order for a coastal survey vessel. The Defence Secretary understands the apprehensions of DTI Ministers, in connection with the impression which could be created by the sale of a controlling interest in Brooke Marine (or any other warship yard) to an overseas Government. This could all too easily provide the critics of privatisation with a ready-made focus for opposition. On balance, and noting that the stated Omani interest is in taking a large majority stake in Brooke Marine, he is inclined to agree that the stake should be limited to one which does not give a controlling interest to overseas investors. Whether or not a minority stake as high as the 30-40% suggested in Ruth Thompson's letter would meet the object of the restriction will depend on how ownership of the remaining 60-70% is split: the Omanis could still end up in effective control.

On the question addressed in paragraph 9 of Ruth Thompson's letter (restrictions on onward sales) Mr Heseltine is content with the DTI proposals as they affect the case of Brooke Marine. But he will wish to consider carefully whether this line will be sufficient in the case of the main warshipbuilding yards.

I am copying this letter to the Private Secretaries to the Chancellor of the Exchequer, the Foreign and Commonwealth Secretary, the Secretary of State for Trade and Industry and Sir Robert Armstrong.

*Yours ever*  
*Simon Lowe*  
 (S H LOWE)  
 Private Secretary

Andrew Turnbull Esq

*Shipman*

MINISTRY OF DEFENCE  
MAIN BUILDING WHITEHALL LONDON SW1

Telephone 01 930 7073



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9 OCT 1984



Treasury Chambers, Parliament Street, SW1P 3AG

M C McCarthy Esq  
Private Secretary to the  
Secretary of State for Trade and Industry  
Department of Trade and Industry  
1 - 19 Victoria Street  
London SW1E 6RB

8 October 1984

Dear Callum

**BRITISH SHIPBUILDERS: DISPOSAL OF BROOKE MARINE**

The Chief Secretary has seen a copy of your letter of 20 September to Andrew Turnbull. He would be content for your Secretary of State to proceed as he proposes in relation to the issues raised by possible foreign bids for Brooke Marine. He presumes that the assurances which he would ask BS to seek from prospective purchasers about their intentions not to on-sell the company, would relate to possible on-sales to foreign rather than domestic purchasers.

2 I am sending a copy of this letter to the Private Secretaries to the Prime Minister, Secretary of State for Foreign and Commonwealth Affairs and Secretary of State for Defence and to Sir Robert Armstrong.

Yours sincerely  
Richard Broadbent

R J BROADBENT

Not Ind : Shipbuilding h7

- 8 OCT 1984



CONFIDENTIAL

cc:ATO



Foreign and Commonwealth Office

London SW1A 2AH

4 October 1984

Dear Andrew,

Answer  
MOD+HMT  
Comments

British Shipbuilders: Disposal of Brooke Marine

Ruth Thompson copied to us her letter of 20 September to you about the disposal of Brooke Marine. I am writing to confirm that the Foreign Secretary is content for British Shipbuilders to proceed as proposed.

We do not anticipate any major problems with the Omanis since the decision not to allow them to buy a controlling stake in the company is clearly non-discriminatory. It will, however, be important to explain the position fully to them. Also, we do not foresee any difficulties, in terms of our EEC Treaty obligations, since there is at present no proposal for restrictions on the acquisition of the company or shares in it by nationals or companies of EC Member States.

I am copying this letter to the Private Secretaries of the Secretary of State for Trade and Industry, Chancellor of the Exchequer and Sir Robert Armstrong.

Yours ever,

Peter Ricketts

(P F Ricketts)  
Private Secretary

Andrew Turnbull Esq  
10 Downing Street

CONFIDENTIAL

- 4 OCT 1984

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Господи, дай им  
Господи дай им





NEW ST. ANDREWS HOUSE  
ST. JAMES CENTRE  
EDINBURGH EH1 3SX

Rt Hon Peter Rees QC MP  
HM Treasury  
Parliament Street  
LONDON  
SW1P 3HE

28<sup>th</sup> September 1984

Dear Peter,

W.  
2/2

FERGUSON/AILSA LTD

Norman Lamont sent me a copy of his letter to you on 25 September about 2 Canadian orders for the Ferguson yard at Port Glasgow of Ferguson/Ailsa Ltd. This yard and the firm as a whole have much improved their performance and efficiency in the last 2/3 years, and I strongly support Norman's view that we should back them with the modest amount of soft credit proposed, together with the guarantee for the second vessel, and I urge you to agree.

Copies of this letter go to the other members of E(A), Geoffrey Howe, Douglas Hurd and to Sir Robert Armstrong.

Yours sincerely,  
George.



NAT IND A7

Shiptonbury

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12 OCT 1984



From the Minister of State for Industry

DEPARTMENT OF TRADE AND INDUSTRY  
1-19 VICTORIA STREET  
LONDON SW1H 0ET

Telephone (Direct dialling) 01-215) ..... 5186  
GTN 215) .....  
(Switchboard) 215 7877

NMPM AT 2579 CENO

Norman Lamont MP

CONFIDENTIAL

Rt Hon Peter Rees MP  
HM Treasury  
Treasury Chambers  
Parliament Street  
LONDON  
SW1P 3AG

25 September 1984

*Dear Peter*

PROSPECTIVE ORDERS FOR BRITISH SHIPBUILDERS FERGUSON YARD

I have been approached by British Shipbuilders with a request for the provision of Intervention Fund and soft credit in respect of two prospective orders from Canada. The particulars are as follows:-

- (a) One anchor handling tug/supply vessel for John Townsend of Canada

Contract price - £4.37m

Support required:

	% Contract price	Amount £
"Standard" aids		
Export Credit Subsidy	11.7	511,290
Intervention Fund	15.0	655,500
Shipbuilders' Relief	2.0	87,400
	28.7	1,254,190
"Exceptional" aid		
Interest make-up agreement	3.0	129,080
	31.7	1,383,270

MONAIS



(b) One anchor handling tug/vessel for Arctic Offshore Marine Services of Vancouver

Contract price - £4.5m

<u>Support required:</u>	% Contract price	Amount £
"Standard" aids		
Export Credit subsidy	11.7	526,500
Intervention Fund	15.0	675,000
Shipbuilders' Relief	2.0	90,000
Total "standard" aid	28.7	1,291,500
"Exceptional" aid		
Interest make-up agreement	3.0	135,000
Total aid	31.7	1,426,500

For the Townsend vessel only BS would be required to give a guarantee of £940,000 in respect of a bank loan to Townsend to cover the 20% of the contract price which Townsend would have to pay BS on placing the order. BS would be given adequate security for this guarantee.

I hope you will agree to these arrangements. The subsidies involved are well within the levels implied by our decision to seek to raise the Intervention Fund intensity limit to 30%. The contracts have been under negotiation for some time and are therefore covered by the IF tranche which expired at end-June this year. The unused balance of that tranche is more than sufficient to cover the requirements of these two orders.

BS are not aware of any EC competition for either order, the amount of soft credit required is modest and therefore the risk that the EC Commission would discover that soft credit is involved should be pretty small.

The Ferguson yard need the orders: steelwork is due to run out in November this year and fitting out in January 1985. You will recall that it is the Ailsa yard of the Ferguson/Ailsa company which BS have it in mind to close.

My intention is that the subsidies involved in these two contracts and any losses that BS might incur on them would be subject to the new control system my officials are devising for limiting BS' financing of individual orders in line with the desired path on merchant capacity.

MONAIS



I am sending copies of this letter to other members of E(A),  
Geoffrey Howe, Jim Prior and Sir Robert Armstrong.

*Yours  
Norman*

NORMAN LAMONT

25 SEP 1984





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B/F with Treasury  
FCO + MOD comments  
A chase within a week. AT 21/9

DEPARTMENT OF TRADE AND INDUSTRY

1-19 VICTORIA STREET

LONDON SW1H 0ET

TELEPHONE DIRECT LINE 01-215  
SWITCHBOARD 01-215 787422

Secretary of State for Trade and Industry

20 September 1984

Andrew Turnbull Esq  
Private Secretary to the  
Prime Minister  
10 Downing Street  
London SW1

Dear Andrew,

BRITISH SHIPBUILDERS: DISPOSAL OF BROOKE MARINE

Following Cabinet's decision in July that British Shipbuilders (BS) should dispose of their warshipbuilding activities, the Corporation has begun to get on with the task. However, we have not yet decided what restrictions if any should be placed on purchases by overseas interests, although since the yards vary considerably in their degree of sophistication and in their importance to our defence interests, a case by case approach may well be appropriate.

2 But we need to decide very quickly what restrictions (if any) to place on foreign ownership of Brooke Marine. BS hope to sell this yard first. They are almost ready to issue the sales document, but do not wish to do so until we can give them a firm steer on foreign ownership.

3 Brooke Marine is situated in Lowestoft and employs about 700 people. It builds patrol vessels, landing craft and other naval craft mainly for export to the Governments of developing Middle Eastern countries, although the MOD is an occasional customer for small vessels such as the Coastal Survey Vessel now on order.

4 BS have told officials that there has been an expression of interest from an agent acting on behalf of an unspecified arm of the Omani Government. Apparently the Omani government would be interested in taking a large majority stake or perhaps even in buying Brooke Marine outright. The possibility of other overseas interest cannot be ruled out, but at present BS are not aware of any. As far as the Omanis are concerned, it appears that they wish to control their own shipbuilding and provide a shipbuilding service to fellow members of the Gulf Co-operation Council. They

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could achieve this either by building their own shipyard or by buying an existing yard, such as Brooke Marine, of whom they are recent customers.

5 There are three separate questions - foreign ownership, foreign and Government ownership, and ownership or part ownership by the Omani Government. Officials here have consulted their opposite numbers in the Foreign and Commonwealth Office and the Ministry of Defence.

6 Neither Department has objected in principle to the idea of foreign control of Brooke Marine, though obviously certain countries or individuals would be unacceptable. There are no security or defence reasons against allowing Brooke Marine to be sold to an acceptable purchaser from a friendly overseas country, though we intend to ask BS to keep us particularly closely informed of any overseas expressions of interest so that we may consider whether they are likely to prove unacceptable in the national interest.

7 Somewhat different considerations apply to the sale of Brooke Marine to another Government, and especially to the Omanis. On the one hand Omani involvement could increase the sale proceeds and lead to a more secure future for the yard. On the other hand it could be difficult to defend an outright sale to another Government. Such a sale would not appear to be compatible with the principle of privatisation. Furthermore, a sale to a Middle Eastern Government could give rise to difficulties in the future.

8 On balance, therefore, Ministers here are opposed to the outright sale of Brooke Marine or, by extension, of any other warship yard, to an overseas Government. It follows that they do not believe that the Omanis should be allowed to buy a controlling stake in Brooke Marine. Although this will be unwelcome to the Omanis, it can be explained that this is because the Government had decided in principle against sales to foreign Governments. On the other hand they do not think that the Government should object to the Omani Government acquiring a minority stake - perhaps in the range 30% - 40% - if they so wish. This could encourage them to place work in the yard.

9 Ministers have also considered whether any special restriction should be placed on onward sales. There is a slight risk that, without such a restriction, the Omanis (or other foreign interests) might acquire control of the yard soon after its privatisation. On the other hand, no such restrictions existed before nationalisation in 1977 and it is unlikely that the Omanis in particular would take a controlling stake against the wishes of HMG. Ministers here therefore consider that it will be sufficient that the Government is not responsible for a direct sale to a foreign Government and accordingly do not intend to retain special share or similar

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powers. But they do propose to ask British Shipbuilders to require the purchaser to confirm that it is not their intention to sell the company on to anyone else.

10 I would be grateful if you would confirm that the Prime Minister sees no objection to allowing BS to proceed with the privatisation of Brooke Marine in the way I have described.

11 I am copying this letter to the Private Secretaries to the Chancellor of the Exchequer, the Foreign and Commonwealth and Defence Secretaries and Sir Robert Armstrong.

*Yours ever,*

A handwritten signature in cursive script that reads "Ruth".

RUTH THOMPSON  
Private Secretary

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Shipbuilding  
Pt 7

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21 SEP 1984

COMPTON



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P.01386

PRIME MINISTER

Harland and Wolff Limited  
(E(NI)(84)11)

BACKGROUND

A  
When the Ministerial Sub-Committee on Nationalised Industries last discussed Harland and Wolff (H & W) in February (E(NI)(84)2nd Meeting, Item 2) they decided:

- to note, without endorsing, H & W's future strategy proposals, which included an aim to secure orders for a wider range of vessel types and sizes;
- that H & W should continue to seek orders on terms similar to those available to British Shipbuilders (BS) including a normal maximum intensity of 30 per cent for assistance from the Intervention Fund;
- to note that H & W and consultants were examining the feasibility of a smaller yard strategy;
- to set a provisional External Financing Limit (EFL) for H & W of £37.5 million for 1984/85;
- to seek European Community (EC) agreement to a maximum intensity of assistance from the Intervention Fund for bulk carriers over 70,000 deadweight tons (dwt) of 35 per cent, at a level of £20 million per annum.

B  
2. In his minute to you of 28 August, the previous Secretary of State for Northern Ireland reported that H & W had signed a letter of intent with British Petroleum (BP) for the construction of a new design of vessel known as SWOPS (Single Well Oil Production System). SWOPS is a 54,000 dwt vessel which will be used to exploit marginal

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seabed oil deposits. The contract price for the vessel is £77 million, excluding owner extras, but including incentive payments of £7.5 million for timely delivery. The proposed subsidy is just over 36 per cent of the contract price, including full incentive payments. It will be slightly higher if soft finance is made available on the full contract price (note 3 to Annex A to E(NI)(84)11), and significantly higher, as a proportion of the price, if delivery is late so that the full incentive payments are not made.

3. The BP order would not provide production work at H & W until mid/late 1985. After completion of four Blue Star ships for delivery in 1985, and the conversion of a container ship for the Ministry of Defence (MoD), H & W's order book is virtually bare. There will therefore be a gap in H & W's workload, at an estimated cost of at least £11 million for keeping the workforce together, unless another order, involving early steelwork, is secured quickly. The only suitable order currently in prospect is from the British Steel Corporation (BSC) for a 173,000 dwt bulk carrier. The terms for this ship would involve a subsidy of just under £14 million, or 48.9 per cent of the selling price. The Secretary of State for Northern Ireland's memorandum, E(NI)(84)11, makes it clear that he sees the two orders as an inter-dependendent package. Taken together, the total subsidy level is just under 40 per cent, assuming the orders are completed on time.

4. Assistance for the BP order requires European Community approval; the position of the BSC order is less clear.

Proposals

5. The Secretary of State for Northern Ireland asks the Sub-Committee:
- a. to authorise H & W to enter into the proposed contracts with BP and BSC;
  - b. to agree that, in return, H & W be instructed to live within its 1984/85 EFL of £37.5 million, and to base its 1985/86 and



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and 1986/87 plans on the availability of maximum public support of £35 million and £30 million respectively and to look for ways of reducing these figures;

c. to postpone a final decision on 1985/86 support levels until H & W's updated business assessment and an analysis of the small yard strategy become available;

d. to agree to notify the BP order to the Commission, but not the BSC order, pending a review by officials.

C  
6. In his minute to you of 5 September (commenting on Mr Prior's earlier minute), the Chief Secretary, Treasury expressed concern about the level of subsidy involved. He points out that if delivery dates are not met this will be well above the levels which Ministers agreed in February. He also argues that acceptance of the orders would preclude adoption of the smaller yard strategy for two years. He therefore proposes:

a. an examination of the scope for renegotiating these orders, and for finding alternative work;

b. if this is impracticable, approving the orders only in return for explicit and quantified improvements to H & W's productivity and EFL targets;

c. agreement on a contingency plan for a smaller yard, or closure, to be activated by agreed criteria.

MAIN ISSUES

7. There is little doubt that the subsidy level involved in the package is higher than the Government would ideally like. The average over the two orders, nearly 40 per cent, is greater than the levels agreed last February - 30 per cent for BS and H & W, and 35 per cent for H & W's larger bulk carriers (relevant only to the BSC order). The main issues are:



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- i. whether the orders should be accepted on the terms proposed;
- ii. if so, whether further improvements in H & W's financial performance should be made a condition of approval;
- iii. the timing of further work on the smaller yard option;
- iv. whether to notify the orders to the Commission.

The terms of the orders

BP order

8. I understand that the Treasury accept that, although high, the level of subsidy for the BP order, if it is delivered on time, is reasonably consistent with what E(NI) agreed in February. However, the figure rises to 45.8 per cent, near the Blue Star level, if delivery dates are not met. The Chief Secretary will probably argue that the chances of an overrun are quite high, since SWOPS is a completely new design. Mr Hurd's memorandum stresses, in paragraph 5, the advantages of the deal's structure, which involves BP bearing the risk on the novel specialist offshore equipment, and he is satisfied that H & W can deliver to time. The Sub-Committee may nevertheless wish to probe the scope for persuading BP to accept more of the risk, for example on the dynamic positioning equipment.

BSC order

9. The proposed level of subsidy for the BSC order - 48.9 per cent - seems clearly higher than agreed by E(NI) in February, even for bulk carriers. It is not clear whether this order, which is a repeat of one in 1982, has been out to tender. The bulk carrier sector is a particularly competitive one, although not so depressed as some other areas, and Mr Hurd holds out no prospect of improvement in the order terms. The Sub-Committee may wish to consider whether there would be any implications for BS of accepting such a high level of subsidy on this order, although BS do not build very large bulk carriers. Is it worth paying such a high price to keep H & W's workload going until

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work starts on the BP order? The other option would be to continue to see whether an alternative intermediate order could be secured at lower subsidy and, if not, to accept the cost of leaving the workforce idle during the gap in work. The quantifiable cost (£11 million) is less than the subsidy on the BSC order (£14 million). There would however be adverse effects on productivity.

#### Benefits of accepting the orders

10. Ministers have accepted that the case for the preservation of H & W rests on political and social grounds. Failure to secure these orders (or alternatives) would almost certainly lead to a sharp, major run-down of the workforce to the point where closure would be seen as inevitable. The signature of the letter of intent for the BP order is public knowledge; the collapse of the order would be bound to attract considerable attention, particularly in the light of Ministerial changes in the Province.

11. Mr Hurd sees the BP order as consistent with H & W's strategy of securing orders for a wider range of vessels. If successful, it could give H & W an advantage in securing further work of this type. Over £40 million of sub-contracts for other United Kingdom (UK) companies are involved.

#### H & W's future financial performance

12. There is unlikely to be much disagreement that H & W should be pressed to continue with its cost-cutting efforts. Mr Hurd proposes to hold H & W to its provisional 1984/85 EFL of £37.5 million, and to instruct Mr Parker, H & W's Chairman, to budget for a cash requirement at or below £35 million in 1985/86 and £30 million in 1986/87. As demonstrated in Annex C of E(NI)(84)11, this represents a continuing reduction in funding levels, and is below the level proposed in H & W's corporate plan. The Chief Secretary may however be looking for greater savings, and might press for more clearly defined productivity targets.

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Smaller yard strategy

13. Work on the smaller yard strategy favoured by the Chief Secretary was originally to have been completed by mid-Summer, but has been delayed by work on the BP and BSC orders. Other members of the Sub-Committee may share the Chief Secretary's disappointment that the study is still not available, and wish to press Mr Hurd to agree to an earlier target for completion than his suggestion of "by Christmas". It seems unlikely that the study can now be completed in time for the Sub-Committee to consider this option in detail before taking final decisions on the BP and BSC orders.

14. Although Mr Hurd says that this timescale will allow decisions on the study to influence final decisions on H & W's funding for 1985/86, acceptance of these two orders will in practice, as the Chief Secretary argues, restrict any effective moves towards a smaller yard until 1986-87. Does the Sub-Committee accept Mr Hurd's argument that the two new orders will provide an opportunity to lay detailed plans for controlled implementation of any rundown?

EC dimension

15. The Sub-Committee will probably be content to accept Mr Hurd's proposal that officials should examine the question of notification of the BSC order. There seems no alternative to notifying the BP order.

HANDLING

16. You will wish to ask the Secretary of State for Northern Ireland to introduce his paper. The Chief Secretary, Treasury could then be invited to explain his concerns on public expenditure. The Secretary of State for Trade and Industry may wish to comment on the implications for British Shipbuilders. The Secretary of State for Energy may have views on the importance of the SWOPS technology, and the likelihood of BP being prepared to renegotiate.

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CONCLUSIONS

17. You will wish the Sub-Committee to reach conclusions on the following:

i. Whether the BP and BSC orders should, at least in principle, be accepted.

ii. Whether any attempt should be made to negotiate improved terms for either or both orders.

iii. If the orders are approved in principle, whether to make approval conditional on acceptance by H & W of improved productivity and/or EFL targets, and, if so, what those targets should be.

iv. Whether the deadline for completion of the smaller yard study should be Christmas, or some earlier date.

v. Whether to notify the BP order to the Commission, but defer notification of the BSC order pending further study by officials.

*PLG*

P L GREGSON

17 September 1984

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Prime Minister 14/9

MR TURNBULL

(Cabinet Office brief  
to come)

14 September 1984

cc Mr Redwood

HARLAND & WOLFF - ORDERS FROM BP AND BSC

E(NI), 18 SEPTEMBER 1984

1. E(NI) should treat these two available orders separately. It will undoubtedly help HW to have the BSC order to provide continuity of steelwork before the BP order can start, but this is another case of "would be nice" rather than "must have".

2. The BSC order is the weaker proposition. The customer is as bankrupt as the supplier, so, looking at it from the taxpayer's point of view, the true subsidy is 100%. In these circumstances, the Prime Minister might start by asking Mr Tebbit whether BSC needs and/or can afford the vessel.

Even in shipbuilding only terms, this is not a good deal. Officials think that the subsidy level, at 48.92%, is higher than for the previous identical ship. (There is a problem of comparability here which I have asked them to clarify.) The negotiated price has fallen from £28.9 million to £28.5 million despite a hardening of charter rates. To approve Mr Hurd's proposal would treat HW very

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much more generously than E(NI) was prepared to treat British Shipbuilders' merchant shipbuilding activities.

So we suggest that Mr Hurd should go back and tell HW to work on a subsidy level no higher than before. Precedent is the only fig leaf of decency which will stick even to that expenditure.

3. The BP SWOPS order has at least some presentational attractions. It is a novel ship design, and it should, by adding to HW's technical expertise, give them competitive advantage for further orders. Conversely, it is possible to foresee nationalistic outcry if clever stuff like this is procured from overseas yards which are thought to enjoy even heavier subsidies than HW.

We fully support the Chief Secretary's view that HW must manage the project so tightly as to earn the incentive payments which BP have offered. John Parker has transformed management systems at HW, so he should not object if Mr Hurd tightens the screw. After Lear Fan and De Lorean, NIO cannot afford their own version of Scott Lithgow.

With this proviso, we would support Mr Hurd's subsidy proposal.

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The Strategy for HW

4. There is no objective method which would enable E(NI) to find the optimum trade-off between subsidy reduction and keeping the workforce (and therefore large parts of Belfast) quiet. Gradualism seems right. We therefore agree that Mr Hurd's proposed maximum EFL's of £37.5 million, £35 million and £30 million - all in cash terms, over the next three years - should be adopted.

R.J.

ROBERT YOUNG

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E(NI) Fddw.

AT 13/9

Br 7/9

PRIME MINISTER

HARLAND & WOLFF: SWOPS ORDER FOR BP

I have seen James Prior's letter of 28 August to you seeking your agreement and that of colleagues to the financing package which will enable Harland & Wolff to secure, inter alia, an order for a Single Well Oil Production System (SWOPS) vessel from BP. I have also seen Peter Rees' minute of 5 September expressing his reservations.

My department is concerned only with the SWOPS project, although I entirely take the point that the two orders are inter-dependent. The SWOPS vessel is a revolutionary design and will be capable of both extracting and shipping oil; it will be the first of its kind to be built. BP plan to use the vessel to develop a number of small oilfields on the UK Continental Shelf. The BP project is of vital importance to the national interest. Not only will it help provide continuity of employment at Harlands but it will also benefit UK manufacturers and suppliers as the bulk of the equipment will be procured from UK sources. It will put UK manufacturers in the forefront of this new area of technology - and thus meet one of our major policy objectives - and it could well lead to further work for Harlands. BP have already hinted that they may wish to order a second vessel to charter to other oil companies.

There is no doubt in my mind that the placement of the contract to build this novel production vessel at Harlands is of vital importance and it is inconceivable to me that the order for this highly sophisticated vessel should go abroad through lack of Government support. I hope very much, therefore, that the financing arrangements outlined in Jim Prior's letter will be approved.

I am copying this to other E(NI) colleagues, the Secretary of State for Foreign and Commonwealth Affairs and Sir Robert Armstrong.

SECRETARY OF STATE FOR ENERGY

13 September 1984

Shipbuilding Pt 7



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FROM: CHIEF SECRETARY  
DATE: 5 September 1984

PRIME MINISTER

HARLAND AND WOLFF LTD (H&W)

In his minute of 28 August Jim Prior seeks your and colleagues' agreement that H&W should take two orders, from BP and BSC. He sees these orders as interdependent.

2 The deal proposed cannot be reconciled with our agreed guidelines for this yard, and would not be acceptable for a BS yard. I believe we should meet to discuss them. There is no reference to how the deal fits in with the objectives of Mr Parker's corporate plan which we approved earlier this year. The subsidy for the two orders combined is a little above the limits we have set on what I believe to be the correct accounting presentation: it will be far above it if (as we have to expect) delivery targets for the BP vessel are not met. As to EFLs, if the distorting effect of soft credit is removed we are offered no improvement as between 1984-85 and 1985-86, contrary to the declining profile we are looking for. But I am above all concerned that the smaller yard strategy, which was to be ready by midsummer, has been held up by work on these orders - which, by keeping the workforce at its present size, would preclude any option of putting that plan into effect for about two years.

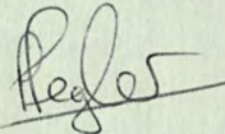
3 It is common ground that a substantial and continued reduction in current levels of support must be a precondition of keeping H&W in operation. The present proposal seems to me inconsistent with that aim. I believe we should discuss the scope for renegotiating the terms of this deal: the BSC order has an unacceptably high subsidy cost, but the BP one is actually worse in terms of the work content that

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the subsidy buys, since so much is to be bought in. We should also discuss the scope for finding alternative work for the yard. If both of those are out of the question, then I believe we should only consider approving the deal in return for explicit and quantified improvements to H&W's existing productivity targets, leading to a more sharply declining EFL profile, and a properly thought-through contingency plan for a smaller yard, with agreed criteria which should activate that plan or a more drastic alternative.

4 I am copying this minute to other E(NI) colleagues, Geoffrey Howe and Sir Peter Armstrong.

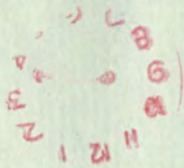


PETER REES

(Approved by the Chief Secretary  
and signed in his absence)

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Not ind: Ship-building A77.



5 SEP 1984

1984





Prime Minister

HARLAND AND WOLFF LTD (H&W)

1. I should like to seek your and colleagues' agreement to authorise H&W to take two orders, one from British Petroleum (BP) and one from the British Steel Corporation (BSC). In shipyard work terms the orders are inter-dependent and I believe we should consider them as a single package. It is a package which would provide the company with a stable production base through to 1986/87 and offer us the clear prospect of a reducing level of public funding over the same period.

BP

2. BP has sought international tenders for an entirely new design of vessel called SWOPS (Single Well Oil Production System). SWOPS is a 54,000 dwt vessel which will be used to exploit marginal seabed oil deposits by, in effect, sucking up the oil through an adjustable nozzle lowered from the surface to connect with the well-head. In the initial round we insisted for the sake of fair competition that H&W's bid was based on the same aid terms as Cammell Laird's but in the event BP shortlisted only H&W, and a Japanese and French yard.

3. The terms proposed for the order, for which H&W and BP have signed a letter of intent, are in my view well within acceptable subsidy limits and, in particular, safeguard H&W against severe penalties for deficient construction or late delivery. The subsidy involved would amount to 36.0% of selling price (as compared with about 48% for Blue Star ships); the only unusual elements are an extra 5% Intervention Fund aid, the substitution of incentive payments for penalties and interest-free loans with a subsidy value of 4.3%. Details are set out in Annex A.

4. The terms negotiated by Mr Parker also provide for the establish-

..../ ment of



ment of a joint management team in which BP experts in offshore construction would be closely involved with H&W in supervising building work; H&W have also retained specialist companies to handle the highly specialised offshore and dynamic positioning elements. More importantly, however, H&W has persuaded BP to accept risk of design, procurement and commissioning of the specialist offshore equipment of the ship and its risk will, therefore, be confined to the hull, propulsion unit and dynamic positioning equipment. These arrangements should undoubtedly help H&W to execute the order efficiently, and at relatively low risk considering the new technology involved.

5. H&W is now the sole UK bidder for this advanced technology order from a British company. I would be most unhappy to see the order, over £40m worth of sub-contracts for other UK companies, and the associated new technology go abroad, probably to France. It is in the national as well as the local interest that this order should go to H&W.

BSC

6. H&W's current order book is mainly for four Blue Star ships for delivery in 1985 (steelwork preparation already mostly completed) and the conversion of a container ship to an aviation training ship for the Ministry of Defence (predominantly outfitting work). The SWOPS order would not provide production work at H&W until mid/late 1985, and this would result in unacceptable gaps in the workload, particularly in steelwork, throughout 1985, peaking at some 800 (out of 1100) steelworkers and costing about £11m. In addition there would be further unquantified costs arising from loss of productivity etc. If therefore the workforce is to be held together in preparation for the SWOPS order, it is essential that the company win an intermediate order, and preferably one on which steelwork can commence immediately.

7. The only order in prospect for the immediate term is from BSC



for a 173,000 dwt bulk carrier - a repeat of one ordered in 1982. The terms for this ship which will be leased from Lloyds Leasing are set out in Annex B and entail a subsidy level of 48.9% - allowing for changes in interest rates, about the same as for Blue Star. I recognise that this is a higher requirement than we have been aiming for. Taking the two orders together, however, the total subsidy is under 40% and the block of work which they represent would provide the company with a stable production base through to 1986/87, giving management the opportunity to continue the introduction of improvements promised in the Corporate Plan.

8. The BSC and SWOPS orders are inter-dependent: without BSC the yard would scarcely be able to gear itself up for the SWOPS contract and in the meantime the additional costs referred to in paragraph 6 above would be incurred. I therefore believe that we should authorise both orders as a single package which will make a major contribution to the regional economy and thus to our political stance in the Province. The alternative, in the absence of any other orders, is an accelerating run down, beginning immediately and leading towards closure. We have considered this course before and rejected it because of the unacceptable effects on the regional economy.

#### Smaller Yard Strategy

9. Earlier this year I agreed with the Chief Secretary to initiate a study of the costs/benefits of a radical slimming down of H&W with a view to a substantial cut in its public expenditure support requirement. It was also agreed that an analysis of the study would be considered in the context of a review of the company's 1984/85 funding.

10. The sensitivity of this study meant that it had to be confined to a very small team of senior management, all of whom have also been involved in the negotiations with BP and BSC. I have therefore



only recently received a draft of the study. At first glance it does not appear to have adequately covered all the ground and it will be some time before officials can present us with an analysis. We cannot however hold up a decision on the BP and BSC orders on this account.

11. Having said this, I share Peter Rees' essential aim, underlying his call for a smaller yard study, of achieving savings in H&W's overall support costs. The company has achieved considerable success in reducing its support costs in the last 3 years - down by 26% in cash terms to a provisional £37.5m in the current year. I see no danger of this provisional figure being exceeded this year. Given the past performance of the yard, this is an encouraging and in some respects remarkable result. In very difficult world conditions, real improvements are being effected. There is still a long way to go, but in seeking permission for these orders I stress that the funds will be provided within the Northern Ireland block and are not additional. I propose to use the opportunity presented by the above orders to tell Mr Parker that he must find scope for further cost-cutting and a continuation of the reducing trend in the annual cash limit. In particular I intend to tell him that in drawing up his plans for 1985/86 and 1986/87 he should know that I will not be willing to recommend to my colleagues an EFL greater than £35m and £30m respectively in those two years, inclusive of grants payable from the Intervention Fund. Initial discussions with the company suggest that these limits will be tough in themselves, particularly for 1986/87. I will nonetheless be stressing to Mr Parker that these are absolute maximum figures and that he should urgently explore and report to me on the scope for further significant EFL reductions which we could consider collectively when we review Mr Parker's business plan update in due course.

#### EC Dimension

12. Under Community law notification of the SWOPS order to the



Commission seems inescapable because of the French competition and because it would require an increase in the rate and volume of the Intervention Fund. The BSC case is more delicate. My officials are already in contact with their DTI, FCI and Treasury colleagues on this and I propose to instruct them to ensure that decisions on notification of the BSC order are in line with the handling of analogous cases for British Shipbuilders.

### Recommendations

13. I recommend that we:-

- (a) authorise H&W to enter into contracts with BSC and BP as described;
- (b) agree to notify BP SWOPS to the Commission and instruct officials to consider the Community dimension of the BSC order in the light of our handling of BS cases;
- (c) agree to instruct Mr Parker, in return for the two orders, to base his plans for 1985/86 and 1986/87 on the availability of £35m and £30m respectively at maximum in public expenditure support; and
- (d) agree to decide on 1985/86 support levels in due course in the light of Mr Parker's updated business assessment and an analysis of the small yard strategy.

14. I am copying this minute to other E(NI) colleagues, Geoffrey Howe and Sir Robert Armstrong.

*Graham Sandford*

JP

(approved by the Secretary of State and signed in his absence)



H&W: BP SWOPS

TERMS OF SUPPORT

	£m	% of Price
Construction Cost (Note 1)	<u>93.9</u>	
Contract Price (Note 2)	<u>77.0</u>	
Intervention Fund	15.4	20.0
Shipbuilders' Relief	1.54	2.0
Interest Subsidy of S.10 loans (NPV) - (Note 3)	7.50	9.74
Interest free loans (NPV) - (Note 4)	3.31	4.29
Total Aid	<u>27.75</u>	<u>36.03</u>

NOTES:-

1. The estimated construction cost of the ship is £96.4m. Offset against this, H&W expects to earn interest of £2.5m from instalment payments received from BP ahead of need.

2. The contract is unusual in its treatment of penalty payments. Instead of the normal arrangement involving payments by a builder to an owner for late delivery (subject to force majeure and contract termination after an agreed period) the two companies have agreed to a lower basic contract price plus incentive payments of £7.5m for timely construction. The contract price shown above includes these incentive payments of which £0.5m is payable on achievement of a key stage during construction, £4m at the end of one year after the due delivery date and £3m at the end of two years after the due delivery date. Late

/ ... delivery



delivery will result in a proportional loss of the post delivery incentive payments for each year. Force majeure - including delays attributable to BP - will apply to the due delivery dates and to the contract termination point.

3. Interest subsidy based on a S.10 loan of 80% of basic contract price excluding post delivery incentive payments ie £70m, at an interest rate of  $7\frac{1}{2}$  repayable over  $8\frac{1}{2}$  years from the date of delivery. The calculation assumes commercial interest rates of 12% and a discounting rate of 13.875%, BP intends to apply for a S.10 loan on £77m; should this be approved, the support would rise by £0.75m to £28.5m, 37% of contract price.

4. H&W proposes to make interest free loans to BP of £5m and £3m. The first loan will be advanced one year after delivery and be repayable after 10 years; the second loan will be advanced two years after delivery and be repayable after 11 years. The calculation is based on interest foregone for the period of the loans at a rate of 12% per annum and a discounting rate of 13.875%.

5. The contract price does not include any amount for owner extras which have still to be defined and could increase both the construction cost and price by £2/3m. The effect would be to increase the amount of direct aid (Intervention Fund, Shipbuilders' Relief and S.10 credit) but not its ratio to contract price.



H&W: BSC

TERMS OF SUPPORT

	£m	% of Price
Construction Cost	<u>37.00</u>	
Contract Price	<u>28.50</u>	
Intervention Fund	7.98	28.0
Shipbuilders' Relief	0.57	2.0
Interest Subsidy on S.10 loans (NPV) (Note 1)	3.05	10.72
Soft Credit (NPV) - (Note 2)	1.79	6.28
Interest Support Agreement (NPV) - (Note 3)	0.49	1.71
Balloon Payment (NPV) - (Note 4)	0.06	0.21
	<u>13.94</u>	<u>48.92</u>

NOTES:

1. Interest subsidy based on a S.10 loan of 80% of contract price at an interest rate of 7½% repayable over 8½ years from the date of delivery. The calculation assumes commercial interest rates of 12% and a discounting rate of 13.875%.

2. Soft credit based on a commercial loan of 20% of contract price as increased by loans necessary to meet the first four instalments of the S.10 loan. The loans are repayable over 8½ years after a 2 year moratorium at a rate of 7½%. The calculation assumes commercial interest rates of 12% and a discounting rate of 13.875%.

3. The interest support agreement is a guaranteeing by H&W that cash balances in the lessor's books arising from the lease will earn interest at the rate of 13% and that the lessor will pay interest on borrowings at 13%. Any excess interest earnings or shortfall in

/ ... interest





interest payments will be paid to H&W. The calculation assumes commercial borrowing rates of 12% and deposit rates of 11%.

4. The balloon payment is a sum of £0.625m payable by H&W to the lessor at the end of the 16 year leasing period. Full provision is made for this payment although the allocation to H&W of 25% of the residual of the vessel (being sought by H&W) could equal a substantial part of the payment. H&W is also required to make a payment of £0.2m to the lessor on delivery of the vessel but it is expected that this sum will be equalled by interest earned on instalment payments received from the lessor ahead of need.

5. Under the terms of the lease, BSC is required to pay a sum of £1.23m to the lessor on delivery of the ship. In consideration for this payment, H&W is proposing to repay to BSC a bonus payment of £0.98m received from the lessor of BSC no 1 under the terms of the contract for that ship.

NAT IND: Shipbuilding Pt 7

CC 10



DEPARTMENT OF TRADE AND INDUSTRY  
1-19 VICTORIA STREET  
LONDON SW1H 0ET  
Telephone (Direct dialling) 01-215 5186  
GTN 215 .....  
(Switchboard) 215 7877

From the Minister of State for Industry

Norman Lamont MP

NBPM  
AK

CONFIDENTIAL

Rt Hon Peter Rees MP  
Chief Secretary  
HM Treasury  
Treasury Chambers  
Parliament Street  
LONDON SW1P 3AG

9 August 1984

Dear Chief Secretary,

BRITISH SHIPBUILDERS - PROSPECTIVE ORDERS FOR SMITH'S DOCK AND GOVAN

Thank you for your letter of 27 July.

I confirm that £70m of Intervention Fund support over two years is compatible with Scenario 3 and that this figure is sufficient to cover the two orders in question. On this basis, I have told British Shipbuilders that we have agreed the financial packages they have proposed. However, I have made our agreement conditional on the relevant features of the orders being compatible with the aid regime that will be introduced as a result of our current negotiations with the Commission. This is a device designed to provide us with a reasonable defence in case the orders are challenged by the Commission.

I am, however, concerned by the interpretation of the E(A) decisions implied by Para 5 of your letter. On this interpretation BS would be required to achieve the contraction envisaged by Scenario 3 year by year starting with 1984/85. What Norman Tebbit proposed, and E(A) agreed however, is that we should work towards that Scenario over the Corporate Plan period. Your interpretation would moreover mean that we must be satisfied that each order is consistent with achieving the year by year Scenario 3 contraction. Such an approach would cut across the approach proposed in Norman Tebbit's paper to E(A) that we should try to avoid becoming involved in decisions on individual orders, relying instead on financial constraints to induce BS to follow the desired path.

MONADZ



I accept, of course, that there must be an effective financial constraint consistent with the E(A) decision and my officials will shortly put forward to yours proposals about this.

I am sending copies of this letter to the Prime Minister, other members of E(A) and to Alick Buchanan Smith.

*Yours sincerely*

*Kate Rhind*

for NORMAN LAMONT

*(approved by Mr Lamont and  
signed in his absence)*

MONADZ

NAT IND: Shipbuilding: Pt 7



19 AUG 1984

*CENO*

DEPARTMENT OF ECONOMIC DEVELOPMENT

STURTELL  
MASSEY AVENUE  
BELFAST  
BT4 2UP

Telephone 63244

Rt Hon Nigel Lawson MP  
Chancellor of the Exchequer  
Treasury Chambers  
Parliament Street  
LONDON  
SW1P 3AG

*NBPW*  
*OK*  
*7/8*  
August 1984

*Dear Nigel,*

HARLAND AND WOLFF PAY 1984-85

Your letter of 27 July to Norman Tebbit sought Jim Prior's views on the recent pay award at H&W. As Jim is on leave I am replying on his behalf.

Norman was quite right in saying, in his letter of 13 July, that H&W had settled at 6%. He did not, however, elaborate on the agreement on extensive changes in working practices which underlay the settlement. These include further flexibility between trades, provision for double day-shift arrangements and strike-free working in ship repair. Management, which believes that the agreement marks a very important step forward, claims that the award will be self-financing and, through PA Management Consultants, we shall be monitoring the implementation of the working practice changes to ensure that as far as possible, they are rigorously prosecuted.

The 1984-85 award must also be seen in combination with the 1983-84 round. You will recall that BS then settled at £7 a week linked to productivity improvements and they believe that this contributed to containing the increase in their 1983-84 wage bill to 0.5%. H&W at that stage settled at 4% (equivalent to £5 a week for a skilled employee), without major productivity links, and this helped towards a 1983-84 wage bill decrease of between 5-6%. I might add that H&W had to withstand increased negotiating pressure because of the stance struck by BS.

I believe that overall the awards conceded by H&W over the past two rounds are not at all out of line with those at BS; and indeed they were achieved at considerably less cost in terms of industrial disruption.

CONFIDENTIAL

Rt Hon Nigel Lawson MP

I should like to make one further point. While recent increases awarded have, overall, been on a par with BS's settlements, pay levels at H&W remain well below those at BS. Prior to the 1983-84 settlements (the last period for which we have data), H&W wages were up to 9% below BS levels.

I am copying this letter to the Prime Minister, Norman Tebbit, George Younger and Tom King.

*Yours in*  
*Adam*

ADAM BUTLER

Shipbuilding: NAT ind R7.





CCND  
NSPM  
AT  
3017

Treasury Chambers, Parliament Street, SW1P 3AG  
01-233 3000

27 July 1984

The Rt Hon Norman Tebbit MP  
Secretary of State for Trade and Industry

*Norman*

**BRITISH SHIPBUILDERS' PAY 1984-85**

You wrote to me on 13 and 25 July about the course of these pay negotiations. In all the circumstances the outcome strikes me as just about satisfactory.

I note what you say about Harland and Wolff and am glad that the repercussions of that settlement on the BS negotiations appear to have been slight. But 6 per cent is a large settlement by the standards of this pay round, and I should be grateful for Jim Prior's comments.

Copies of this letter go to the Prime Minister, Jim Prior, George Younger and Tom King.

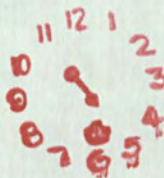
*Nigel Lawson*

NIGEL LAWSON

NAE IND P57

Shepherd

30 JUL 1984





Treasury Chambers, Parliament Street, SW1P 3AG

Rt Hon Norman Tebbit MP  
Secretary of State for Trade & Industry  
Department of Trade & Industry  
1 Victoria Street  
LONDON  
SW1E 6RB

27 July 1984

*Stan Norman*

**BRITISH SHIPBUILDERS - PROSPECTIVE ORDERS FOR SMITH'S DOCK AND GOVAN**

Thank you for your letter of 23 May. *July?*

I entirely agree that the E(A) conclusion was that, as you put it, we should avoid as far as possible becoming involved in decisions about the future of individual yards, and should rely instead on the financial constraint imposed by a tight limit on the total amount of subsidy available for contract financing to induce BS to follow the desired scenario.

The problem I have is that there are as yet no finally agreed financial constraints. In their absence we are driven back either to taking a view on individual orders and hence on the future of individual yards or to seeking to agree, pending our discussions in the autumn, suitable financial figures within which to frame our decisions.

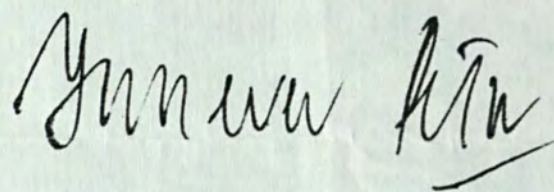
Table 2 attached to your paper to colleagues in E(A) does provide some reasonably clear figures for the desired scenario (ie scenario 3). And I take it that these figures are also consistent with the proposed figure of £70 million intervention fund support for the next 2 years which you recommended colleagues to go for in the Brussels' discussions.

It would be consistent therefore with the approach agreed by E(A) Committee to allow BS to accept orders which do not prejudice the scenario 3 figures in table 2 (or an intervention fund provision of £70 million over the next two years) and I would be prepared to do this. However the table 2 figures clearly require the main part of the contraction of BS merchant shipbuilding to be achieved this year, if the later year figures are not to be exceeded. Are we clear that the acceptance

of either of these orders, and particularly perhaps the Smith's Dock one, would still permit this? If not, then I believe one or both must be turned down.

In short, if you are satisfied that acceptance by BS of these orders is consistent with achievement of the financial projections associated with the desired scenario then I have no further objection to make. If on the other hand one or both of the orders would cause these projections to be exceeded in advance of our expenditure discussions in the autumn, then acceptance would not in my view be compatible with the decisions we have reached.

I am sending a copy of this letter to the Prime Minister, other members of E(A) and to Alick Buchanan-Smith.



PETER REES

Nat Ind Snippmiding

27 JUL 1984



NBP 07  
AF 2817

MR TURNBULL

26 July 1984

PROSPECTIVE ORDERS FOR BRITISH SHIPBUILDERS  
C. Y. TUNG FOR GOVAN  
B.U.E FOR SMITH'S DOCK

This minute is intended for your own use only.

The mounting pile of correspondence between DTI, D/En and Treasury over these two prospective orders is leading nowhere. The delays look pretty bad from every point of view, and I guess that the Prime Minister may have to break the deadlock - absurd though it is that she should become involved in minor matters.

In the case of the C. Y. Tung prospect for Govan, DTI's proposition is to sell for little over £23 million a perfectly conventional ship which will cost nearly £33 million. The BUE/Smith's Dock proposition, engineered jointly in DTI and D/En, is to sell more than £17 million of ship for under £14 million, on terms of Byzantine complexity. Both prospective orders are stated to be in the national interest.

On objective grounds Treasury are quite right to resist. They need help to do so.

1. Govan/C. Y Tung

Firstly, if Govan is a 'core yard' of BS, why is its prospective performance not better? A core yard surely should not be one which needs a handout of over 40% to stay in business?

Secondly, there is a speciousness about the argument that the 'extra' subsidy involved (£3 million) is less than the £6 million of overheads it would recover. If Govan don't take Mr Tung's order, they can eliminate some over-heads.

Thirdly, it is not clear:

- i. what happens to BS' commitment to a £7 million balloon payment if the lease collapses within 15 years; or
- ii. what happens if the EC objects retrospectively to the excessive level of Intervention Fund offered.

CONFIDENTIAL

2. BUE/Smiths Dock

This is the most 'iffy' proposition we have seen for a long while. The argument appears to run as follows:

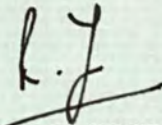
- If
- i. BUE Ships secures a diving services contract from Hamilton Bros;
  - and ii. BUE Ships orders a complex vessel on Smith's Dock in order to fulfil the contract;
  - and iii. BS builds the vessel for £17 million but sells it for £13 million;
  - and iv. BS subsidises a commercial bank loan to BUE ships;
  - and v. BS guarantees £5 million for at least four years as part security for the bank loan;
  - and vi. the vessel performs;
  - and vii. BTG sells part of its majority shareholding in BUE Ships' parent to a minority shareholder;
  - and viii. BTG raise new equity in BUE to dilute further BTG's own stake;
- then BTG might then be able to dispose of its holding in BUE. When, and for how much, is not clear.

This seems to me like trying to become a nurse because you like grapes!

The risks and rewards are wildly out of proportion, and the interventionist intentions of DTI and D/En grossly out of tune with the Government's determination to make its own corporations behave commercially.

3. We recommend no more than existing levels of aid to either prospective contract.

If either goes ahead on the terms proposed, we will have encouraged the shipbuilding industry in the belief that the old psychology and never ending subsidy are acceptable. We will also have set back E(A)'s decision of last week to cut BS' merchant capacity to a third of its current level.

  
ROBERT YOUNG

- 2 -

JMHABQ

CONFIDENTIAL

E. R.  
NAT IND  
PT 7 Shipbuilding  
with AT

PRIME MINISTER

SHIPBUILDING

Mr. Tebbit's statement today did not raise great passions. The Opposition's talk of privatisation of warship building was fairly routine.

Attached is a copy of the statement, together with speaking notes on the main points which arose.

25 July 1984



## SPEAKING NOTES

### Closures

British Shipbuilders' Corporate Plan contains no plans to close shipyards. But the future of any shipyard in the UK depends upon its ability to obtain new orders and build ships to time and to cost. The Chairman of British Shipbuilders is aiming for new orders of about 200,000 tons this year. Whether he succeeds depends on the success of British Shipbuilders competing in the world market.

### Inadequate Support for British Shipbuilders?

The Government has provided over £1.1 billion in support of British Shipbuilders since 1979, over £20,000 per employee. It is now up to British Shipbuilders to put its operations on a more competitive footing.

### 1983/84 Losses

Last year British Shipbuilders lost £117 million and this year £161 million. Of that loss Scott Lithgow contributed £75 million and the Government agrees with the Chairman of British Shipbuilders that a better performance next year is essential.

### Warship Building Privatisation

The Manifesto upon which the Government fought and won the Election proposed the privatisation of substantial parts of British Shipbuilders. This decision gives effect to that pledge.

/Effect on

Effect on Merchant Shipbuilding of Privatisation

British Shipbuilders merchant shipbuilding interests must survive and compete on their own merits. Merchant shipbuilding cannot be cross-subsidised from the defence budget.



Secretary of State for Trade and Industry

BRITISH SHIPBUILDERS STATEMENT

---

MR SPEAKER, WITH PERMISSION I WILL MAKE A STATEMENT ABOUT BRITISH SHIPBUILDERS.

THE CORPORATION TODAY PUBLISHED ITS ANNUAL REPORT AND ACCOUNTS FOR 1983/84.

COPIES HAVE BEEN LAID BEFORE THE HOUSE.

1

JH2ATX



Secretary of State for Trade and Industry

cc P. office

THE CORPORATION MADE A TRADING LOSS OF £161M OF WHICH £75M WAS CONTRIBUTED BY SCOTT LITHGOW, WHICH IS NOW IN THE PRIVATE SECTOR FOLLOWING THE SUCCESSFUL RESCUE OPERATION IN MARCH.

THE CHAIRMAN HAS STATED, AND I AGREE, THAT THE CORPORATION CANNOT ACCEPT A CONTINUATION OF THE LAST TWO YEARS' PERFORMANCE.

I WELCOME HIS ASSURANCE THAT POLICIES HAVE NOW BEEN ESTABLISHED TO ENSURE THAT THE PRINCIPAL LOSSES SHOULD NOT BE REPEATED.

2

JH2ATX



Secretary of State for Trade and Industry

I ALSO WELCOME THE STEPS THAT THE CORPORATION HAS BEGUN TO TAKE ON THE RATIONALISATION AND RESTRUCTURING OF ITS ACTIVITIES.

ON 4 JUNE I RECEIVED THE CORPORATION'S PROPOSED CORPORATE PLAN FOR THE PERIOD 1984/85 TO 1978/88 AND I AM PLACING IN THE LIBRARY A VERSION WITH COMMERCIALY CONFIDENTIAL INFORMATION DELETED.

3

JH2ATX

V5788



Secretary of State for Trade and Industry

THE GOVERNMENT ENDORSES THE CORPORATION'S PRIMARY AIM OF CONCENTRATING RESOURCES ON A STABLE, COST-EFFECTIVE MAINSTREAM MERCHANT SHIPBUILDING BUSINESS.

THE CORPORATION IS WELL AWARE THAT THE KEY TO ITS FUTURE DEPENDS ON IMPROVING THE EFFICIENCY OF PRODUCTION OF MERCHANT SHIPS.

IT SEES THE PRIMARY NEED AS BEING THE CONCENTRATION AND INTEGRATION OF ITS PRODUCTION, SERVICE AND ADMINISTRATIVE FACILITIES TO INCREASE EFFICIENCY, FLEXIBILITY AND PRODUCTIVITY.

4

JH2ATX

V5788



Secretary of State for Trade and Industry

IN ALL THIS A FURTHER KEY ELEMENT WILL BE THE IMPLEMENTATION OF THE FLEXIBLE WORKING PRACTICES AGREED WITH THE WORKFORCE EARLIER THIS YEAR.

THE HISTORY OF SUCH ATTEMPTS TO SAVE, LET ALONE, REVITALISE, MERCHANT SHIPBUILDING IS NOT ENCOURAGING.

5

JH2ATX

V5788



Secretary of State for Trade and Industry

THE NEW PROGRAMME IS AMBITIOUS IN ITS SCOPE BUT IT IS ESSENTIAL, AND IT IS SUPPORTED BY THE GOVERNMENT.

THE CORPORATION PLANS TO BE ABLE TO ACCEPT ORDERS AT A RATE OF UP TO 180-210,000 CGRT A YEAR.

THIS CONTRASTS WITH THE 117,000 CGRT OF ORDERS WON IN 1983/84.

THE HOUSE WILL APPRECIATE THAT THE CORPORATION'S ABILITY TO WIN ORDERS AT SUCH A RATE WILL DEPEND ON A NUMBER OF FACTORS.

6

JH2ATX

V5788



Secretary of State for Trade and Industry

THESE INCLUDE THE STATE OF THE WORLD MARKET;  
THE AGREEMENT OF THE EUROPEAN COMMISSION TO AN  
ENHANCED RATE OF SUBSIDY THROUGH THE  
INTERVENTION FUND; THE SIZE OF THAT FUND; THE  
DEGREE TO WHICH PRODUCTIVITY IS IMPROVED; AND  
THE EXTENT TO WHICH COMPETITIVENESS IS  
INCREASED.

THE GOVERNMENT WILL TAKE DECISIONS ON FUNDING  
LEVELS IN THE AUTUMN IN THE LIGHT OF THE  
NEGOTIATIONS IN BRUSSELS.

7

JH2ATX



Secretary of State for Trade and Industry

I HAVE ALREADY WARNED THE CORPORATION THAT A  
TIGHT FINANCIAL REGIME WILL HAVE TO APPLY,  
AND THAT FUNDING LEVELS WILL DEPEND ON THE  
OVERALL PUBLIC EXPENDITURE POSITION AT THE  
TIME.

IN THE LIGHT OF OUR MANIFESTO COMMITMENT TO  
PRIVATISE A SUBSTANTIAL PART OF BRITISH  
SHIPBUILDERS THE GOVERNMENT HAS DECIDED THAT  
BRITISH SHIPBUILDERS SHOULD SELL THEIR  
WARSHIPBUILDING INTERESTS, MAKING SUBSTANTIAL  
PROGRESS TOWARDS PRIVATISATION BY 31 MARCH  
1985 AND COMPLETING IT BY 31 MARCH 1986.

8

JH2ATX



Secretary of State for Trade and Industry

THE CORPORATION WILL ALSO CONTINUE TO DISPOSE OF OTHER SALEABLE ASSETS.

ACCORDINGLY I HAVE TODAY ASKED THE CORPORATION TO SET IN HAND ACTION TO DISPOSE OF THOSE PARTS OF THE CORPORATION ENGAGED MAINLY OR WHOLLY IN WARSHIPBUILDING.

TO SECURE THE MAXIMUM PRACTICAL EXTENT OF FAIR COMPETITION WE WOULD PREFER TO SEE THE YARDS SOLD SEPARATELY OR IN SMALL GROUPS.

9

JH2ATX



Secretary of State for Trade and Industry

I HAVE, HOWEVER, ALSO ASKED THE CORPORATION TO SET IN HAND CONTINGENCY PREPARATIONS FOR A FLOTATION ON THE STOCK EXCHANGE OF ALL OR SOME OF THE COMPANIES IN CASE INDIVIDUAL SALES MAY NOT BE ACHIEVED.

I BELIEVE THAT THIS WILL ENABLE THE CORPORATION TO PURSUE SINGLE MINDEDLY THEIR AIMS FOR THEIR MERCHANT SHIPBUILDING BUSINESS AND TO TAKE THE STEPS TO IMPROVE EFFICIENCY ON WHICH THEIR LONG-TERM FUTURE DEPENDS, WHILE PROVIDING AN ASSURED COMPETITIVE WARSHIPBUILDING CAPABILITY.

10

JH2ATX



NBPM AG 25/7 a.d.

DEPARTMENT OF TRADE AND INDUSTRY  
1-19 VICTORIA STREET  
LONDON SW1H 0ET

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(Switchboard) 215 7877

From the Minister of State for Industry

Norman Lamont MP

The Prime Minister  
10 Downing Street  
LONDON  
SW1

25 July 1984

*Dear Prime Minister see p. 145*

When I wrote you on 23 November last giving my latest monthly report on the finances of the Shiprepairing Division of British Shipbuilders, I promised to let you have a report on the position at the end of the financial year.

As you know, BS disposed of Grangemouth late last year and Tyne Shiprepair was taken over, after some doubts on the part of its labour force, by a group of its managers in February. Falmouth has now been offered for sale and it is likely to have numerous interested buyers. In the case of Vospers we were committed to await the completion of the Saudi royal yacht 'Abdul Aziz'. This is now delivered and plans for the sale of the yard are well in hand.

The financial outcome yard by yard for the financial year 1983/4 is as follows.

Trading profit (loss)	£
Falmouth Shiprepair Ltd	773,000
Vosper Shiprepairers Ltd	457,000
Grangemouth Dockyard Ltd (to 3 November 1983)	(172,000)
Tyne Shiprepair Ltd (to 5 February 1984)	(5,195,000)
	<hr/>
	(4,137,000)
	<hr/> <hr/>





Both Falmouth's and Vosper's profits would have been the better but for industrial action at the end of 1983, which, in the case of Vosper, lost it the 'Canberra' refit to the continent. The losses quoted at the two yards now sold exclude costs arising from the writing down of fixed assets and other extraordinary costs of closure: these are £1.3 million at Grangemouth and £3 million at Tyne Shiprepair.

*Yours*  
*Norman*  
NORMAN LAMONT

1984



CC NO



DEPARTMENT OF TRADE AND INDUSTRY  
1-19 VICTORIA STREET  
LONDON SW1H 0ET  
TELEPHONE DIRECT LINE 01-215 5422  
SWITCHBOARD 01-215 7877

Secretary of State for Trade and Industry

NBEM  
AT  
25/7

25 July 1984

The Rt Hon Nigel Lawson MP  
Chancellor of the Exchequer  
HM Treasury  
Parliament Street  
London SW1P 3AG

D. Nigel.

BRITISH SHIPBUILDERS: PAY SETTLEMENT

In my letter of 13 July I told you that British Shipbuilders were hoping to reach a pay settlement with their unions when they met them on 16 July.

2 This they did. The unions accepted a pay deal which is estimated to cost 3.9% on the corporation's pay bill. Taken together with other marginal movements on conditions, the increase in average earnings is about 4.2%. This is in line with the basis on which the existing EFL was predicated.

3 Graham Day warned me that the unions would inevitably try to put the deal in a more favourable light by making very optimistic (from their viewpoint) assumptions of the value of some marginal improvements in sick pay etc included in the package. This they have indeed done and you may have seen reports of a 4.75% deal. However, Graham Day is quite clear that the representative cost of the pay deal is 3.9%.

4 This means that he has come out with a settlement at the level for which he aimed. It embodies the reinforcement of differentials he was seeking and, although not directly linked to productivity, it does carry with it agreement to reconvene a National Working Party on productivity improvement which stopped meeting during last year's pay battles. And, provided the deal is ratified promptly by the yards, he will also have achieved his aim

JH2ATP



of a quick clean settlement and getting a potential major problem out of the way.

5 I am sending a copy of this letter to the Prime Minister, Jim Prior, George Younger and Tom King.

A handwritten signature in black ink, appearing to read 'Norman Tebbit', with a horizontal line underneath the name.

NORMAN TEBBIT



NBSM

AT 25/7

Treasury Chambers, Parliament Street, SW1P 3AG

Ruth Thompson  
Private Secretary to  
the Secretary of State for Trade and Industry  
Department of Trade and Industry  
1 Victoria Street  
LONDON  
SW1H 0ET

24 July 1984

De. R.H

**BRITISH SHIPBUILDERS: ORAL STATEMENT**

I am writing to confirm the amendments we proposed over the phone to the draft statement you circulated yesterday. They were all to page 2 of the draft and were as follows:

Para 2, second sentence - delete "to the future of the industry"

Para 3, final sentence - delete "and the future levels of funding of the corporation by the Government"

Final para, redraft to read - "The Government will take decisions on funding levels in the Autumn in the light of the negotiations in Brussels. They will depend on the overall public expenditure position, but I have already warned the Chairman that it will be necessary for British Shipbuilders to operate within a tight financial regime."

In addition, Treasury Ministers agree with the Prime Minister's comment.

I am sending copies of this letter to Andrew Turnbull, Murdo Maclean, Janet Lewis Jones, and David Hayhoe.

Yours sincerely

J. Gieve

JOHN GIEVE

25 JUL 1984



Handwritten markings in the bottom right corner, including the letters 'VL' and some illegible characters.

HMT  
NIO  
D/N  
SO  
WO  
D/En  
LPS  
DTI  
CDL  
D/M

MAFF  
CST  
TRANS  
CO

bc. Bob Young

*NH*



10 DOWNING STREET

*From the Private Secretary*

24 July 1984

*Dee Ruth,*

*- oral? Yes*

British Shipbuilders: Oil Statement

The Prime Minister has seen a copy of the draft oral statement your Secretary of State proposes to make on British Shipbuilders on 25 July. She is generally content but feels that the middle paragraph of page two needs to be looked at further. As drafted, this could give the misleading impression that the Government is endorsing a forecast of 180-210,000 cgrt., or regarding it as a level of orders which is likely to be achieved. You may wish to consider making a contrast between capacity of 180-210,000 cgrt and British Shipbuilders' ability to win orders to fill that capacity according to the factors listed in the second half of the paragraph.

I am copying this letter to Private Secretaries to Members of E(A), Richard Mottram (Ministry of Defence), Murdo McLean (Chief Whip's Office), David Beamish (Lords' Whips Office), and to Lord Lucas' Private Secretary.

*Yours sincerely  
Andrew Turnbull*

Andrew Turnbull

Miss Ruth Thompson,  
Department of Trade and Industry

*ls*

CONFIDENTIAL

CC 24



JU849

Secretary of State for Trade and Industry

DEPARTMENT OF TRADE AND INDUSTRY

1-19 VICTORIA STREET

LONDON SW1H 0ET

Telephone (Direct dialling) 01-215

5422

GTN 215

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23 July 1984

Rt Hon Peter Rees MP  
Chief Secretary  
HM Treasury  
Parliament Street  
London SW1P 3AG

NBPM

AT 24/7

BRITISH SHIPBUILDERS - PROSPECTIVE ORDERS FROM BUE AND TUNG

Thank you for your letter of 12 July 1984. Following the E(A) discussions on British Shipbuilders' strategy we need to take substantive decisions on these two cases. They are both urgent: BUE for reasons which have been rehearsed in previous correspondence, and Tung because BS need to tell its customers by 27 July whether or not the deal is on.

2 An important feature of the strategy which E(A) agreed is that we should avoid as far as possible becoming involved in decisions about the future of individual yards, relying instead on the financial constraint imposed by a tight limit on the total amount of subsidy available for contract financing to induce BS to follow the desired scenario. It would not be consistent with this approach to seek to impose an additional criterion designed to deflect orders away from certain yards. The essential point is that whatever subsidy went into a particular order and a particular yard would diminish the amount left for other orders and yards.

3 Even so, on any reasonable assessment of yard importance and performance Govan would undoubtedly qualify for inclusion in whatever list of core yards might be drawn up. The subsidy involved for the Tung order is high but, as the attached table shows, the figure is within the IF intensity of 30% we have agreed should be negotiated with the EC Commission and not very different from the 25% that E(A) agreed we might need to settle for.

4 To reject the BUE case now would not only cut across the approach approved by E(A) that we should avoid becoming involved in decisions about the future of individual yards. It would also involve a real risk of our being accused of engineering the closure of Smiths Dock, a charge which would not be easy to refute.





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5 The subsidy involved, at 5.4% of contract price above current levels, is well within the extra 15% on IF intensity we have agreed should be negotiated with the Commission. And while the required BS guarantee is substantial we must not assume that it would inevitably give rise to additional costs. I believe it would be well worth taking a calculated risk of its being called, not least because of BUE's importance as a wholly UK underwater engineering company operating in the offshore sector, a point which Alick Buchanan-Smith has strongly emphasised, and the implications of a rejection for the prospects of a successful privatisation of the firm.

6 The point about adverse publicity is the very simple one that it would not be easy for my Department, or indeed the Treasury, to explain and defend the delay in determining the Government's attitude to this case.

7 I am sending a copy of this letter to the Prime Minister, other members of E(A) and to Alick Buchanan-Smith.

A handwritten signature in dark ink, appearing to read 'Norman Tebbit', with a horizontal line underneath.

NORMAN TEBBIT

## CONFIDENTIAL

Cost of Package

	<u>Contract of Price</u>	<u>£ million</u>
<u>Standard Aids</u>		
Intervention Fund	15.0	3.50
Shipbuilders' Relief	2.0	0.47
Home Credit (NPV)	11.2	2.61
	—	—
	28.2	6.58
<u>Exceptional Aids</u>		
Additional Intervention Fund	5.4	1.25
Lease Support (NPV)	7.2	1.67
	—	—
	12.6	2.92
TOTAL	40.8	9.50

The the aid percentage above the standard amounts to 12.6%. This compares with the 15% IF increase we are seeking to negotiate with the Commission and the 10% we might have to settle for.

WAT (nt)  
Ruphildy  
WAT

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9 4 1 0  
8 7 6 5 4  
3 2 1

24 JUL 1984

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①

PRIME MINISTER

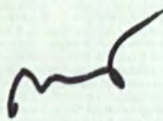
BRITISH SHIPBUILDERS: ORAL STATEMENT

I have one comment on Mr. Tebbit's draft statement. E(A) took a decision not to reduce British Shipbuilders' capacity but to ration the amount of subsidy in the expectation that this would support orders of around 100,000 cgrt, though BS could achieve a higher level if its performance improved. In the light of this the middle paragraph of page 2 could be considered misleading if the E(A) decision were ever made public. The phrase "at the forecast level" could be interpreted as a forecast by Government of orders of 180-210,000 cgrt.

DTI are aware of this. I suggest the point could be met by redrafting the start of this paragraph as follows:

"The Corporation plans to be able to accept orders of 180-210,000 cgrt. This contrasts with 117,000 cgrt of orders won in 1983/84. The rate at which the Corporation will be able to win orders to take advantage of this capacity will depend on a number of factors. These include ..."

MOD are announcing tomorrow the decision to call for new tenders for the Type 22 frigate.



23 July 1984

VSCAEA

CONFIDENTIAL



JU856  
Secretary of State for Trade and Industry

ccRY cc Press office  
TF

DEPARTMENT OF TRADE AND INDUSTRY  
1-19 VICTORIA STREET  
LONDON SW1H 0ET

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GTN 215 .....  
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23 July 1984

Andrew Turnbull Esq  
Private Secretary to the  
Prime Minister  
10 Downing Street  
London SW1

Dear Andrew,

BRITISH SHIPBUILDERS: ORAL STATEMENT

I enclose a copy of a statement my Secretary of State proposes to make on British Shipbuilders on 25 July.

2 I would be grateful for urgent clearance.

3 I am sending a copy of this letter and the statement to the Private Secretaries of Members of the Cabinet, to the Government Whips' offices in both Houses, and to Lord Lucas' Private Secretary.

Yours ever,

RUTH THOMPSON  
Private Secretary

Enc

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JU855

DRAFT STATEMENT

Mr Speaker, with permission I will make a statement about British Shipbuilders.

The Corporation today published its annual Report and Accounts for 1983/84. Copies have been laid before the House. The Corporation made a trading loss of £161m of which £75m was contributed by Scott Lithgow, which is now in the private sector following the successful rescue operation in March. The Chairman has stated, and I agree, that the Corporation cannot accept a continuation of the last two years' performance. I welcome his assurance that policies have now been established to ensure that the principal losses should not be repeated. I also welcome the steps that the Corporation has begun to take on the rationalisation and restructuring of its activities.

On 4 June I received the Corporation's proposed Corporate Plan for the period 1984/85 to 1987/88. I am placing in the Library a version with commercially confidential information deleted. The Government endorses the Corporation's primary aim of concentrating resources on a stable, cost-effective mainstream merchant shipbuilding business. The Corporation is aware that the key to its future depends on improving the efficiency of production of merchant ships. It sees the primary need as being the

CONFIDENTIAL

concentration and integration of its production, service and administrative facilities to increase efficiency, flexibility and productivity. A further key element will be the implementation of the flexible working practices agreed with the workforce earlier this year.

The history of such attempts to save, let alone, revitalise, merchant shipbuilding is not encouraging. The new programme is ambitious in its scope but it is essential to the future of the industry and it is supported by the Government.

The Corporation considers that a realistic market share is consistent with an annual order intake of 180-210,000 cgrt and plan to be able to accept orders of that level. This contrasts with the 117,000 cgrt of orders won in 1983/84. The Corporation's ability to win orders[at the forecast level] will depend on a number of factors. These include the state of the world market; the degree to which productivity is improved; the agreement of the European Commission to an enhanced rate of subsidy through the Intervention Fund; and the future levels of funding of the Corporation by the Government.

The Government will take decisions on funding levels in the Autumn in the light of the outcome of the negotiations in Brussels and of the overall Public Expenditure position at the time.

CONFIDENTIAL

In the light of our manifesto commitment to privatise a substantial part of British Shipbuilders the Government has decided that British Shipbuilders should sell their warshipbuilding interests, making substantial progress towards privatisation by 31 March 1985 and completing it by 31 March 1986. The Corporation will also continue to dispose of other saleable assets.

Accordingly I have today asked the Corporation to set in hand action to dispose of those parts of the Corporation engaged mainly or wholly in warshipbuilding.

To secure the maximum practical extent of fair competition we would prefer to see the yards sold separately or in small groups. I have, however, also asked the Corporation to set in hand contingency preparations for a flotation on the Stock Exchange of all or some of the companies in case individual sales may not be achieved.

I believe that this will enable the Corporation to pursue single mindedly their aims for their merchant shipbuilding business and to take the steps to improve efficiency on which their long-term future depends, while providing an assured competitive warshipbuilding capability.





THE MINISTER OF STATE

DEPARTMENT OF ENERGY  
THAMES HOUSE SOUTH  
MILLBANK  
LONDON SW1P 4QJ

Direct Line 01-211 3290  
Switchboard 01-211 3000

The Rt Hon Peter Rees QC MP  
Chief Secretary  
Treasury Chambers  
Parliament Street  
London  
SW1P 3AG

23. July 1984

Dear Peter,

Thank you for sending me a copy of your letter to Norman Tebbit about the BUE order. Your response raises a number of points to which I feel I must return.

I take the points entirely that the future of Smith's Dock is uncertain. But it was British Shipbuilders, not BUE, who designated Smith's Dock as the yard at which the vessel should be built. BUE are perfectly content to see the order transferred to another suitable yard, eg Govan, if that fits in better with the BS corporate plan. Neither we nor BUE are in any sense wedded to Smith's Dock. So, unless it is the case that one of the long-term options is to eliminate entirely BS' capacity to build vessels of this sort, I would be quite content to see support offered in respect of a build in a different yard. This should, surely, meet your main concern.

My second concern is that you do not seem to give enough weight to the importance in the national interest of the Hamilton order. To say, as you do, that this is an "area of North Sea activities already well served by the Americans and Dutch" thus implying that support for a UK presence in that sector commands no priority is to undermine the whole of our offshore supply industrial support policy. It is precisely because it is an area dominated by the Americans and Norwegians (not the Dutch) that we need to take every opportunity which presents itself to generate a competing UK capability. This contract is a unique starting point which we must not ignore and which it is important to support. I do not need to emphasize how weak our public position would be if we lost the order through lack of Government support.

When I wrote to Nigel Lawson I said that this contract could be the first of several - since then BUE have been approached by Petrobras asking whether they would be interested in bidding for a ten year management contract, involving a similar vessel, the hull to be built in Brazil, but the major share of the equipment to be procured in the UK.

CEWJ

NRPM  
AT  
24/7

12 July



The chances of such a contract actually being placed would be greatly enhanced if BUE can quickly finalise their contract with Hamilton Bros.

I hope, therefore, that even at this late date you could reconsider your position and support the BUE order to be placed at a BS yard, though not necessarily in Smith's Dock.

I am sending a copy of this letter to the Prime Minister, other members of E(NI), Norman Lamont and Sir Robert Armstrong.

*You are*  
*Alick*

ALICK BUCHANAN-SMITH

"NAT WND PT 7 -  
SHIPBUILDING



2 JUL 1984



*Composite version produced for  
PM's chestroom.*

*AT 2/8*

PRIVY COUNCIL OFFICE  
WHITEHALL, LONDON SW1A 2AT

19 July 1984

*Dear Andrew,*

SELECT COMMITTEE ON TRADE AND INDUSTRY: BS CORPORATE PLAN

Thank you for your letter of today's date attaching a form of words for the Prime Minister to use at Questions in the House if the Select Committee's call for BS documents is raised. The Lord Privy Seal would much prefer the attached form of words to be used since it emphasises the existing arrangements which are now to be looked at again in the light of this incident.

I am sending a copy of this letter to Janet Lewis-Jones (Lord President's Office), Hugh Taylor (Home Office), David Peretz (HM Treasury), Callum McCarthy (Department of Trade and Industry), Dinah Nichols (Department of Transport), Michael Reidy (Department of Energy), Murdo Maclean (Chief Whip's Office), Henry Steel (Law Officers' Department) and Richard Hatfield (Cabinet Office).

*Yours sincerely,  
David Morris*

D R MORRIS  
Private Secretary

A Turnbull Esq  
Private Secretary to the  
Prime Minister



As was made clear in the Government's reply to the report of the Liaison Committee (First Report, Session 1982-3), on the Select Committee system, there must always be the possibility that differences of opinion may arise between Ministers and select committees as to whether it would be in the public interest for particular information - whether relating to the nationalised industries or any other public matter - to be disclosed to a select committee. (X)

*Nevertheless* In the final analysis it is for the House as a whole to decide in such instances whether the powers of a select committee should be enforced.

~~The Government will continue to judge these cases on their merits, and will be examining ways of ensuring [redacted] that the disclosure of information to select committees does not prejudice the efficient management of the nationalised industries.~~

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10 DOWNING STREET

*From the Private Secretary*

19 July, 1984.

Select Committee on Trade and Industry: BS Corporate Plan

I attach a form of words which the Prime Minister might use at Questions in the House today if the Select Committee's call for BS documents is raised. I would be grateful for comments on this by 1300 today.

I am sending copies of this letter to Janet Lewis-Jones (Lord President's Office), Hugh Taylor (Home Office), David Peretz (HM Treasury), Callum McCarthy (Department of Trade and Industry), Dinah Nichols (Department of Transport), Michael Reidy (Department of Energy), Murdo Maclean (Chief Whip's Office), Henry Steel (Law Officers' Department), and Richard Hatfield (Cabinet Office).

Andrew Turnbull

David Morris, Esq.,  
Lord Privy Seal's Department.

CONFIDENTIAL

Select Committee on Trade and Industry: BS Corporate Plan

Line to take

EX  
The Government remains of the view that it is not in the best interests of the good management of nationalised industries or of their relationship with their sponsor Departments that documents of the kind requested should be supplied to Select Committees. Nonetheless, the powers of Select Committees, as currently being interpreted, require that such documents should be supplied if requested, and this has been done. The Government believe that if Ministers are to receive from Chairmen of nationalised industries the advice they need to take what are often difficult and painful decisions, new understandings on the power to call for documents need to be reached with the Select Committees.

**GENERAL COUNCIL OF BRITISH SHIPPING**

Telephone: 01-283 2922

30-32 ST. MARY AXE

LONDON, EC3A 8ET

*CP*

18th July, 1984

F.E.R. Butler, Esq.,  
Principal Private Secretary to the Prime Minister,  
10, Downing Street,  
London, S.W.1.

*Dear Robin,* *FERB*

At lunch on Monday, I promised that I would send you our list of other leading maritime countries' subsidisation/protectionism. Here it is.

Thank you so much for coming. We all thought it was a very good occasion. We trust the Prime Minister did too.

I hope my telephone call this morning wasn't "lèse majesté".

*Yours sincerely,*  
*Patrich*

(W.P. Shovelton)



WORLDWIDE SHIPPING SUBSIDISATION/PROTECTION

	<u>Country</u>	<u>Mn. dwt.</u>	
1	Greece	66	Complex system of tax exemptions ranging up to 6 years.
2	Japan	63	Tax-free reserves and special arrangements. Easy credits.
3	Norway.	32	Tax set off against personal income; government pays 50% of seafarers' repatriation expenses; 12 year (3 year moratorium) cheap domestic shipbuilding credit. Seafarers' tax relief.
4	USA	26	Operating and capital construction subsidies. Cabotage reserved.
5	USSR & East Bloc	22+	State-owned - no profit criteria. Direction of cargo.
6	UK	19.5	Nil.
7	France	16	Some subsidies. Form of investment grant, cabotage, reservation of tanker cargoes, COFACE support.
8	Italy	15	Some subsidies. Tax-free reserves. Cabotage.
9	China	13	State-owned - no profit criteria. Extensive reservation of cargo.
10	South Korea	12	Cargo preference. Some subsidies.
11	Spain	12	Import protection. Cabotage.
12	Singapore	11	Favourable credits. Profits tax-free.
13	West Germany	10	Investment grants.
14	India	10	Construction subsidies. Cheap loans. Cabotage. Bilateralism.
15	Netherlands	7	Investment grants. Seafarers' tax relief.
16	Sweden	5	Cheap credits. Seafarers' tax relief.

General Council of British Shipping,  
30-32, St. Mary Axe,  
London, EC3A 8ET.

17th July, 1984

SUBJECT  
a memoJ-ee  
Z

## 10 DOWNING STREET

18 July 1984

*From the Private Secretary*Select Committee on Trade and Industry:  
British Shipbuilders Corporate Plan

The Prime Minister held a meeting this evening to discuss the demand by the Select Committee on Trade and Industry that the Chairman of British Shipbuilders should make available to the Committee by 10.00 am the following morning "the corporate plan as recommended by the Corporation to the Secretary of State for Trade and Industry, together with such other additional material which the Secretary of State has requested the Corporation to prepare and furnish him". Present were the Lord President, the Lord Privy Seal, Home Secretary, Chancellor of the Exchequer, the Secretaries of State for Trade and Industry and Transport, the Attorney General, Chief Whip and Minister of State, Department of Energy.

The Secretary of State for Trade and Industry said that the Chairman of British Shipbuilders, with his agreement, had supplied the Committee with the Corporation's original corporate plan which was based on one projected level of output, but without material on the options which the Secretary of State had requested. The Select Committee were demanding material relating to these options and the papers they were seeking would also contain information on the orders for Type 22 frigates and the future of Cammell Laird. The Committee had offered safeguards on the handling of these documents; they would be seen only by members of the Committee in the Clerk's Office and no copies or notes would be taken. This would not, however, prevent members of the Committee from using the information in cross-examination of witnesses before the Committee or as the basis for PQs in the House.

Mr. Day had originally been reluctant to take advantage of an assurance that the Government would protect him if he refused to supply the material. Unfortunately, he had told the Committee that he was withholding the information sought on the instructions of the Secretary of State and that in the absence of these instructions he would be prepared to comply. Subsequently, following discussions with the Secretary of State he had come to realise that supply of the

documents would harm the relationship with his sponsor Minister.

The Secretary of State for Trade and Industry recommended that the request of the Committee should be resisted although he acknowledged that the Committee would be likely to respond with a special report which would have to be debated early the following week on the floor of the House. He was concerned, not simply with the information involved in the present case, but that this might lead to the Committee demanding highly controversial information in relation to other nationalised industries. It was not possible to conduct the business of a sponsor department if all material passing between the Minister and the chairman of the nationalised industry was subject to disclosure. The Secretary of State for Transport and the Minister of State, Department of Energy argued that to accede to the Committee's demands in this case would create similar difficulties for the industries for which they were responsible. In discussion it was argued that papers from nationalised industries should be treated as advice to Ministers as would be the case with departmental papers.

The Lord Privy Seal and the Chief Whip said the powers of Select Committees were very wide and the Select Committee system would work only if they were operated with restraint. Regrettably that had not been so in this case. Nevertheless they advised that the Government would be unwise to challenge a motion put down by the Select Committee. The ensuing debate would become the focus for backbench discontent on a number of issues. Committee members would argue that what was at issue was whether they could be trusted to adhere to the safeguards they had offered. In current circumstances a vote could probably be won but only with the greatest of difficulty. It would be better to accede to the Committee's request in this instance but to make it clear very soon that the Government did not consider the relationship between Select Committees and Departments which had developed as being satisfactory. They believed that outside the immediate confrontation the Government could negotiate adequate understandings with the Liaison Committee on new Select Committee procedures and a vote on them could be won.

In discussion there was general support for the Secretary of State for Industry on the issue of principle but it was recognised that Mr Day's statements to the Committee made it difficult to withstand the present demand. On the other hand, the question was raised of why the Government could prevail in a discussion in the autumn if it could not prevail now. In reply, it was argued that the debate now would be about adherence to the existing

rules and whether members of Select Committees could be trusted to honour safeguards they had offered; in the autumn the debate would be about whether better conventions could be devised.

Summing up, the Prime Minister said that the meeting had concluded that Mr. Day should provide the Select Committee with the documents it had requested. The Government should, however, make it very clear that it was unsatisfactory for Select Committees to operate in this way both for the relationship of nationalised industries to their sponsor departments and for the management of the nationalised industries themselves. The Government would therefore put new proposals to the House. The Prime Minister invited the Lord Privy Seal, in consultation with colleagues, to advise on how the Government's views should be made known and on how best to go about securing new understandings with the Select Committees on their powers to call for papers.

I am copying this letter to Janet Lewis-Jones (Lord President's Office), David Morris (Lord Privy Seal's Office), Hugh Taylor (Home Office), David Peretz (HM Treasury), Dinah Nichols (Department of Transport), Henry Steel (Attorney General's Office), Murdo Maclean (Chief Whip's Office), Ian Fitzpatrick (Minister of State's Office, Department of Energy) and Richard Hatfield (Cabinet Office). I would be grateful if this letter were retained within Private Offices and shown only to officials who need to know of it in order to carry forward the work on the revised proposals mentioned above.

Andrew Turnbull

Callum McCarthy, Esq.,  
Department of Trade.



CONFIDENTIAL

JU811

PRIME MINISTER

BRITISH SHIPBUILDERS' CORPORATE PLAN

The Trade and Industry Select Committee today has ordered Mr Graham Day, Chairman of British Shipbuilders, to produce before 10.00am tomorrow "the papers described by the Chairman of British Shipbuilders as the Corporate Plan as recommended by the Corporation to the Secretary of State for Trade and Industry together with such other additional material which the Secretary of State has requested the Corporation to prepare and furnish him". The Committee has refused to accept a document previously sent to them by British Shipbuilders, which comprised a bowdlerised plan. They have also rejected an explanation which I discussed at length last night with Kenneth Warren, Chairman of the Committee, with which he expressed himself satisfied.

2 We therefore need to decide, tonight, whether to allow British Shipbuilders to accede to this demand, or whether we are prepared to give the assurances to Mr Day that we shall do all within our power to protect him if he does not. In practice, the first course means that the documents would be lodged with the Clerk of the Committee. On the precedent of Corporate Plans made available to the Select Committee in 1981, it is reasonable to expect that the Committee will give undertakings that no



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copies should be made of the document, and that members of the Select Committee should consult it only in the Clerk's Office. These precautions cannot, of course, prevent those members of the Committee who have access to the Plan and supporting documents from using that information, for example, in relation to PQs and the pursuit of oral PQs on the floor of the House. The second choice would mean that the Select Committee would report to the House that its notice had been served, and not complied with, and it would then be necessary, if we are to protect the Chairman of British Shipbuilders, for us to make clear that the Government would explain that this had been done with its approval, for wider public interest reasons. We could expect a debate, which would take precedence over other business, and it would prove necessary for the Government to marshal all its support against the Select Committee demand. I have no power to direct Mr Day to refuse to provide the information, and, not unreasonably, he will only agree to ignore the Select Committee's demand if he has our assurance that we will act in this way. It is not yet clear that he would be prepared to act as we would need if this course is to be pursued. I attach an annex on the constitutional and procedural points, prepared by the House Officers.

3 I have no doubt that to accede to the demand of the Select Committee would be severely damaging to the relations between the Chairmen of nationalised industries and their sponsoring Secretaries of State. It would be damaging enough in relation to British Shipbuilders; if comparable demands were made in



CONFIDENTIAL

relation to BSC it would be politically even more damaging and embarrassing. For this reason I strongly believe we should be prepared to take the political row and the possible loss of a day's business of the House, in order to preserve what I regard as the essential confidentiality of dealing between Government and nationalised industries.

4 I am copying this to Willie Whitelaw, John Biffen, Nigel Lawson, Michael Havers, Peter Walker, Nicholas Ridley, John Wakeham and Sir Robert Armstrong.

*Ruth Thompson*

PT N T

18 July 1984

Department of Trade and Industry

NOTE ON THE PARLIAMENTARY PRIVILEGE ASPECT

1. The Trade and Industry Committee have made the following Report today (Wednesday) which will be published in the Votes and Proceedings tomorrow:

Trade and Industry, - Mr. Kenneth Warren reported from the Trade and Industry Committee an Order, which was read as follows:

That there be laid before this Committee by the Chairman of British Shipbuilders before 10.00 a.m. on Thursday 19th July 1984, the papers described by the Chairman of British Shipbuilders, in evidence to this Committee [18th July] as "the Corporate Plan as recommended by the Corporation of the Secretary of State for Trade and Industry, together with such other additional material which the Secretary of State has requested the Corporation to prepare and furnish him."

2. The Committee are due to meet again tomorrow afternoon. If the papers have not been received they will be likely to produce a Special Report of the circumstances that evening. They have no powers to impose any sanction on their own authority.
3. Precedence would be sought for a Motion to take the Special Report into consideration, and this would be likely to be granted early next week. At this point, it would be open for Members to advance rival propositions - for example, to summon the Chairman to the Bar on a subsequent occasion to explain his action, or, in the contrary sense, to say that the House would take no further action. Motions and amendments on these lines would be debatable, without any specific time-limit, other than the Ten o'clock rule.
4. There seems no doubt that the Committee have sent for papers that they are technically empowered to send for. The question is whether, on the merits of the case, the House wishes to lend its practical support to what they have done.
5. It will be recalled that in January 1978 the British Steel Corporation complied with a formal request for the following papers, following an initial refusal:



Each quarterly revision between 1st January 1976 and 30th September 1977 of the forecasts as submitted to the Department of Industry of:

1. Application of Funds.
  - 1a. Fixed Assets and Investments.
  - 1b. Working Capital.
  
2. Sources of Funds.
  - 2a. Internally Generated Funds.
  - 2b. Public Dividend Capital.
  - 2c. Foreign Borrowings.
  - 2d. U.K. Borrowings.

of the British Steel Corporation for the financial year 1977-78 in the form in which these figures were submitted to the Select Committee on Nationalised Industries by the Secretary of the British Steel Corporation on 5th October 1976.

C. J. B.

C. J. B.

18th July 1984

18 JUL 1984

12 1 2 3 4 5 6 7 8 9 10 11





10 DOWNING STREET

Prime Minister

Policy Unit strongly support the Tebbati  
line.

As was apparent from yesterday's  
E(A), BS's plans for the merchant  
sector will imply substantial redundancies  
in the North East. To direct workshop  
work to Cannell Laird which it does  
not win in fair competition is to add  
to the redundancies in the North East.

No social case has been made for  
spanning Merseyside and letting the  
North East bear all the burden.

AT

18/7



Ref. A084/2064

PRIME MINISTER

Warshipbuilding Privatisation

FLAG A C(84) 19

## BACKGROUND

FLAGS B+C The Ministerial Sub-Committee on Economic Affairs (E(A) has considered this subject on two occasions (E(A)(84) 11th and 15th Meetings). On both occasions the discussion concentrated almost exclusively on the destination of orders for two Type 22 frigates, on which there was a sharp difference of view between the Secretary of State for Defence and the Secretary of State for Trade and Industry: the Secretary of State for Defence wished to direct at least the first order to the Cammell Laird (CL) yard on Merseyside; the Secretary of State for Trade and Industry wished the order to be the subject of a further round of competitive tendering. It is largely to resolve this difference that the matter has been referred to the Cabinet.

2. But the Cabinet will also need to take decisions on the general approach to the privatisation of warshipbuilding. The Government's Election Manifesto said that it would aim at transferring a 'substantial part' of British Shipbuilders (BS) to the private sector. The privatisation programme endorsed by E(A) earlier this year (E(A)(84) 2nd Meeting) suggested that privatisation should be possible from 1985 onwards.

3. Mr Tebbit's detailed proposals on privatisation are summarised in Annex A to C(84) 19; they are very similar to those which he previously put to E(A). He recommends that all warship yards should be transferred to the private sector. He implies that it would be preferable to sell yards individually or in groups in order to preserve competition. He favours sale to industrial buyers; but in case this should go too slowly, or produce inadequate proceeds, there should be simultaneous work towards a public flotation. The Chairman of BS, Mr Day, should be given the detailed task of negotiating sales, but with unequivocal and detailed instructions on such matters as scope, method and speed. The deadline should be March 1985 (at the end of 1985 if a flotation proves necessary).



4. As background to the discussion Mr Tebbit will wish to report orally to the Cabinet the proposals for merchant shipbuilding approved by the Ministerial Sub-Committee on Economic Affairs today (E(A)(84) 19th Meeting, Item 1). It has been agreed that merchant shipbuilding capacity should be roughly halved over the period to 1987-88 but that there should be no explicit targets for capacity or manpower. It will be for BS to work within the External Financing Limit and the constraints on subsidy negotiated with the Commission; and the restructuring will be, so far as possible, by "part-closure" than by the closure of major yards.

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#### MAIN ISSUES

5. The main issues before the Cabinet are as follows:

(i) Against the prospects for warshipbuilding capacity and orders described in Annexes D and E to C(84) 19, how should the Type 22 orders be dealt with?

(ii) In the light of the decisions taken under (i) above, what should be the Government's approach to privatisation of warshipbuilding? In particular:

(a) Should any yards in Great Britain be retained in the public sector?

(b) Should the Government require overt competition to be maintained by selling different yards, or groups of yards, to different owners; or is a sale to one buyer acceptable?

(c) If a sale to one buyer is acceptable, is flotation an acceptable method? Is it perhaps preferable to a negotiated sale to a corporate buyer?

(d) Who should take the lead in negotiating any sales?

(e) Should the negotiator have a deadline and/or a pre-condition regarding sale proceeds?

Type 22 Orders

6. In the E(A) discussions there has been a difference of view between the Secretary of State for Trade and Industry and the Secretary of State for Defence about warshipbuilding capacity. Mr Tebbit has argued that substantial over-capacity is in prospect and can be avoided only by closing at least one yard. Mr Heseltine has argued that the prospective gap could be partially filled by exports, merchant work and re-fits. Most members of E(A) considered it most unlikely that exports could be won at realistic prices on any scale likely to diminish the problem of over-capacity in the warshipbuilding industry.

7. If the Cabinet also take this view it follows that at least one warshipbuilding yard should close. If BS had a free hand, it seems clear that they would choose to close CL. However, largely for industrial relations reasons they prefer to give CL at least the chance of staying open under the 'alternative strategy' described in Annexes D and E to C(84) 19. Mr Tebbit clearly has misgivings about that strategy; but he recommends going along with it, at least to the extent of allowing CL, with other yards, to submit a further round of competitive tenders for the Type 22 orders.

8. Mr Heseltine has argued against this that CL have won two previous rounds of competitive tenders; that to require the yard to submit to a third round would be widely suspected as being a way of allowing BS to rig the tenders so as to ensure that it closed; and that the social consequences on Merseyside of allowing CL to close would be extremely serious. He therefore proposed to E(A) that the order for at least one Type 22 frigate should be directed to CL, taking their latest previous tender as a basis for negotiation; if the yard performed satisfactorily on that order they would receive the second order.



9. In reaching a view the Cabinet will wish to consider the following points:

(a) BS have always admitted that their 'alternative strategy' for keeping CL open is fragile. The events described in paragraph 7 of C(84) 19 must have made it more so.

(b) There is a difference of opinion as to whether CL can really be said to have 'won' the second round of tendering. It is clear that they submitted what was, if marginally, the lowest price. It also seems clear that the assumptions they made about overheads were falsified by the loss of an expected order, though BS national management did not require them to withdraw the tender on that account; and it has been argued that a private sector concern in a similar position might well have chosen to maintain its quotation and seek extra work to absorb overheads. But it now seems (paragraph 8 of C(84) 19) that CL expects to lose £7.4 million on the Type 22 order if it gets it. It seems hard to deny that whether to allow this sort of loss to be made is a matter for BS's national management (and ultimately the Government as owner and financier of BS). If so, CL's previous tender cannot simply be taken as a basis for negotiation without more ado.

(c) The social consequences of closing CL would indeed be severe. But if the Cabinet consider that warship-building capacity must be reduced, one or more yards will have to be closed. If CL is spared, others will suffer. The Cabinet will need to decide whether the social consequences of this would be less severe.

(d) Whatever happens to warshipbuilding, there will, as E(A) has agreed, be a substantial contraction of merchant shipbuilding with severe employment consequences in the North East in particular. Sparing CL will aggravate this latter problem.



(e) Directing a Type 22 order to CL would not be easy to reconcile with the policy on merchant shipbuilding under which it will be left to BS to decide how best to contract the industry within the financial limits which have been set.

#### Carrying the Costs

10. It was pointed out in the discussion in E(A) that the costs of over-capacity cannot be avoided. All that can be done is to choose whether they appear as excessive contracts prices or as losses on contracts. If the Cabinet should favour directing a Type 22 order to CL and so to prolong excess capacity, it will therefore be necessary to decide where the cost should fall.

Mr Tebbit argues:

(i) that the cost should come out in a higher tender price and so fall on the Defence Budget; and

(ii) that any cost overruns should also fall on the Defence Budget.

11. The Cabinet may well feel that the first of these arguments is fair. The second is less clear cut:

(a) If CL were demonstrably less efficient than other yards and so more likely to suffer cost overruns, there would be logic in making the budget of the Minister who wishes to direct the order to CL bear the financial consequences.

(b) Otherwise, there is no reason to treat an order from CL differently from an order from another yard, with cost overruns, unless otherwise provided by contract, falling on the supplier. To lay it down in advance that they would fall on the customer would give no incentive to efficiency.





## Privatisation

12. No member of the Cabinet is likely to suggest that privatisation of warshipbuilding is undesirable. But the specific proposals in C(84) 19 raise a number of issues:

### (a) Retention of yards in the public sector

It is unlikely to be disputed that the privatisation of all warshipbuilding yards in Great Britain is desirable. It may, however, be questioned whether it is essential, as Mr Tebbit argues. Harland and Wolff compete for naval orders and are unlikely to be either closed or privatised in the foreseeable future; it is not suggested that this is an insuperable objection to privatisation of naval yards in Great Britain.

### (b) Competition

The Cabinet will wish to consider how important an objective competition is, and how it can be achieved. At one extreme it would be possible to argue that closure of yards will reduce competition; and that even some sales of small groups of yards would leave no effective competition; and that therefore no two yards should be sold to the same buyer. At the other, it could be argued that the only effective competition is between yards in this country and yards overseas; that for strategic reasons such competition will generally not be allowed; and that sales of the yards as one entity will probably maximise the sale price and should therefore not be ruled out.

### (c) Method of Sale

The Cabinet's views on the importance of competition will have a bearing on the proposed sale method. If they decide that sale to a single buyer should be ruled out, it would be logical to decide against flotation of warshipbuilding as a single concern.



(d) Responsibility for Negotiations

It is likely to be generally accepted that the Chairman of BS should be made responsible for conducting negotiations with potential buyers, so long as he is given clear objectives.

(e) Objectives for Negotiations

Again, it is likely to be agreed that the negotiator should be given a deadline (Mr Tebbit suggests March 1985, or the end of 1985, if a flotation proves necessary). There may be more argument about whether they should be given a target for the sale proceeds. Treasury Ministers may be briefed to suggest this. If so, other Ministers may argue that there is no harm in setting a figure as an objective, but that it should not be a pre-condition: in other words, final decisions should be taken in the light of all circumstances, of which the prospective proceeds would be one, but not the only one. Certainly it seems reasonable to suppose that the financial benefits of effective competition in warshipbuilding, if it could be achieved, would outweigh any difference in the sale proceeds that might be produced by one method of sale rather than another.

HANDLING

13. It will probably be convenient to divide the discussion into two main parts:

(i) how the order for Type 22 frigates should be dealt with, in the light of the Cabinet's views about prospective capacity and orders in the warshipbuilding industry; and

(ii) privatisation.

The first part might be opened by the Secretary of State for Trade and Industry; you will then wish to invite the Secretary of State for Defence to reply. The Secretary of State for the Environment



will have views on the political impact of decisions on Merseyside and other parts of the country. The Chief Secretary, Treasury will have views on public procurement and public expenditure aspects.

14. The second part of the discussion might also be opened by the Secretary of State for Trade and Industry. Either the Chancellor of the Exchequer or the Chief Secretary, Treasury may have comments, both on particular aspects and from the standpoint of the privatisation programme as a whole. The Secretary of State for Defence will wish to comment on the importance of effective competition among warshipbuilders.

#### CONCLUSIONS

15. You will wish the Cabinet to reach conclusions on the following:

(i) In the light of prospects for warshipbuilding orders and capacity, should the order for Type 22 frigates:

(a) be directed to Cammell Laird; or

(b) be the subject of re-tendering by the three yards previously asked to tender, as proposed in C(84) 19?

(ii) If the order is directed to Cammell Laird, where should any resulting excess costs fall?

(iii) Do the Cabinet agree with the detailed proposals regarding privatisation in C(84) 19, and in particular:

(a) that no warshipbuilding yard in Great Britain should be retained in the public sector;

(b) that yards should be sold individually or in small groups, but that the possibility of a public flotation should be kept open;

(c) that the Chairman of British Shipbuilders should take the lead in negotiation with potential buyers?



(iv) If the Chairman of British Shipbuilders does take the lead in negotiations, what guidelines should he be given?

R

Approved by  
ROBERT ARMSTRONG  
and signed in his absence.

18 July 1984

conqueror

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PRIME MINISTER

17 July 1984

c Mr Redwood

MERCHANT SHIPBUILDING

1. This year, BS' Corporate Plan for merchant shipbuilding is less important than the Board's covering letter. In the latter, the Chairman makes plain that UK merchant shipbuilding cannot become viable for as far ahead as the eye can see. In effect, he is asking Government to decide the future shape and size (if any) of the industry.

2. In reaching their conclusion about non-viability, BS evaluate three main capacity options. Underlying all three are:

- i. the disposal of Cammell Laird whether by sale or closure;
- ii. the withdrawal of Swan Hunter from merchant shipbuilding, so that the yard can be privatised in warship form.

The job losses involved (from today's levels) are about 4,000. But the capacity reduction is essential, and we fully support BS' intentions.

3. The three options provide annual capacity of 200,000 tonnes, 150,000 tonnes and 100,000 tonnes respectively. The results are:

Capacity	Cash outflow 1985/6 to 1987/8 £	Employment
200,000 t	220 m	10,000
150,000 t	197 m	7,000
100,000 t	190 m	5,500

Since this expenditure leads nowhere, we see no point in sanctioning it. (And the lack of difference between the cash outflows suggests a surprisingly high level of yard fixed costs).

4. We judge that the right commercial response to all this is calmly to acknowledge BS' statement of non-viability and let the merchant shipbuilding industry close as it runs out of work. This does not mean that we shall stop building ships. There will still be a hefty warshipbuilding industry

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and a national capability in ship repair - both in the private sector - and there will be Harland & Wolff in Belfast.

5. Of course the location and extent of job losses will be politically sensitive. If the yards close in orderly fashion as work runs out (a rough, rather heroic assumption) the following pattern will emerge:

<u>Location</u>	<u>Job Losses</u>	<u>Period of Closure</u>
Clydeside	3,500	1st Qtr 85 - 2nd Qtr 86
North East	6,000	1st Qtr 85 - 2nd Qtr 86
North Devon	800	1st Qtr 1985
Miscellaneous and HQ	300	1984 and 1985

Against these job losses should be set continuing employment in warshipbuilding:

<u>Location</u>	<u>Jobs</u>	<u>Yards</u>
Clydeside	6,000	Yarrow
North East	6,000	Swan Hunter
Cumbria	13,000	Vickers
Aberdeen	700	Hall Russell
Norfolk	700	Brooke Marine
Southampton	2,000	Vosper

In addition, Scott Lithgow will sustain about 1,000 jobs; the ship repairers around 500; and Harland and Wolff 6,000.

So although we shall lose around 15,000 jobs in merchant shipbuilding between 1984 and 1986, we shall retain 35,000 in warship and other sectors.

6. Mr Tebbit argues against industry closure, and in favour of contraction to 100,000 tonnes. His underlying case rests on manageability rather than on finance, but will be portrayed publicly as the inevitable outcome of EC limits on the volume and intensity of shipbuilding aid. In other words, we will try to shift the blame onto Europe.

Although we fully agree with the need for contraction, we doubt the wisdom of both the hidden and the public case. Firstly, the volume of aid allowed by the EC will become common knowledge. It is then easily translatable into ship orders, so the size of the industry we are prepared to

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contemplate will pretty soon become known. Secondly, is it really simpler and cheaper to manage a clutch of 'part yards' (pipes from one, electricians from another, and so on), than to control a smaller number of 'whole yards' as we currently know them?

If yards do not close, we leave intact the fixed costs, the expectation of further subsidies and orders, and the whole psychology which has kept shipbuilding in being on a scale far bigger than the market needs. Closing yards stops the money drain once and for all.

7. If Ministers wish to reduce or spread the merchant job losses, a perfectly reasonable method might be to leave a pocket of capacity in each traditional shipbuilding area.

Since we will have warshipbuilding on Clydeside and Tyneside, there might be a case for one yard elsewhere in the North East, on Wearside or Teesside (a choice of Austin and Pickersgill, Sunderland or Smiths Dock) and possibly one in North Devon (where Appledore is the sole candidate).

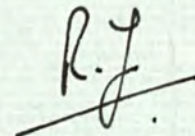
With that kind of capacity reduction, it might actually be possible to return both yards to private ownership.

8. We recommend:

- i. that E(NI) should be prepared to let GB merchant shipbuilding close completely;
- ii. if not, that the industry should be scaled down to one yard on Wearside or Teesside plus Appledore in North Devon;
- iii. that in any event BS should withdraw Swan Hunter from merchant shipbuilding and should be allowed to close Cammell Laird.

The effect of iii. in particular is to create a neat package of warshipyards for privatisation in 1985;

- iv. that presentation of the policy should play up the size and strength of the warshipbuilding and other independent sectors, and play down as inevitable the contraction of merchant.



ROBERT YOUNG

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P.01344

PRIME MINISTER

British Shipbuilders: Corporate Plan 1984/5-1987/8  
(E(A)(84)43)

## BACKGROUND

The Ministerial Sub-Committee on Nationalised Industries (E(NI)) discussed strategic issues for British Shipbuilders (BS) in February (E(NI)(84)2nd Meeting, Item 1). BS's warshipbuilding activities have been discussed twice recently in the Sub-Committee on Economic Affairs (E(A)(84)11th and 15th Meetings).

2. At its discussion in February, E(NI) decided that decisions on the future of merchant shipbuilding and the structure of BS must await the production of a corporate plan and other material by BS. This was to include an assessment by BS of the viability of merchant shipbuilding in the United Kingdom (UK) in the longer-term and an assessment of the sensitivity of BS's financial projections to different rates of productivity growth. Provision for BS for 1985/86 in the 1984 Public Expenditure White Paper was to be drawn to the attention of the Chairman, Mr Day, but he was not to be rigorously constrained to produce his corporate plan in conformity with the published figures.

3. At the same time, the Secretary of State for Trade and Industry was invited to open negotiations with the European Communities (EC) with a view to securing an increase in the intensity of Intervention Fund (IF) aid to 30 per cent at a volume of £100 million over two years (it is now thought likely (E(A)(84)43, paragraph 3) that the EC may agree to IF of 25 per cent, perhaps at a lower volume of £70 million over two years).





4. As in February, the BS Board recommend maintaining civil shipbuilding capacity of 200 kcgrt (thousand corrected gross registered tonnes), the first and highest of three Options illustrated then (Annex A to E(NI)(84)3). Option 2 was 150 kcgrt; Option 3, 100 kcgrt. The BS recommendation is intended to "sustain most of the existing merchant capacity to provide a period of relative stability while warshipbuilding privatisation and other restructuring takes place" (E(A)(84)43, paragraph 4). BS propose that closures of large yards should be avoided by making some specialised facilities serve several yards in the North-East and on Clydeside instead of being provided separately at each yard as at present. In effect, this would replace a policy of few, large closures with one of partial closures on a wider scale.

5. The Secretary of State for Trade and Industry, however, argues that the Government should not tie itself to any particular target for manpower or capacity. BS should, however, be required to work within financial constraints, including tough EFLs, calculated to produce an outcome nearer Option 3 than Option 1. He considers that this would nevertheless allow the Government to endorse the approach adopted in the BS plan of "part closures", rather than closure of major yards.

#### MAIN ISSUES

6. The main issues are as follows.
- i. What should be the future capacity of BS for merchant shipbuilding?
  - ii. How should the target be set?

Commercial Considerations

7. The Board of BS has stated that

"viability, defined as a commercial return on capital employed, is not possible within the plan period" (E(A)(84)43, paragraph 3).

In its view there are no foreseeable circumstances in which such viability can be achieved. Though it would be possible to construct less demanding definitions of viability, it is clear that purely commercial considerations would indicate closure of the merchant shipbuilding capacity of BS.

Non-Commercial Factors

8. Neither BS nor Mr Tebbit recommend total closure. Among factors calling for the retention of some capacity are:

i. Employment

The three options imply the following reductions from the 1984/85 employment figure of about 21,000:

\*Option 1 - 9,000 ⇒

Option 2 - 12,000

Option 3 - 13,800

In February, BS estimated that its merchant division and engine builders together employed about 18,500 people.

ii. Regional Considerations

Yard closures would obviously have particular, regional significance. Closures might have serious

\* Table 2, E(A)(84)43



implications in particular for the North East. Annex E to E(A)(84)43, which shows the location and workload of each BS merchant yard, illustrates this.

iii. Industrial Relations

BS say that "(Scenario 2 and) Scenario 3 in particular would be likely to give rise to industrial disruption and industrial relations difficulties..." (E(A)(84)43, Annex A, paragraph 7.5). This is no doubt true, not only of Options 2 and 3, but of any significant restructuring proposals.

Future capacity

9. Against this background the Sub-Committee may well feel that the right approach is to run down the merchant shipbuilding capacity of BS as fast as the employment, regional and industrial relations considerations permit. Option 3, a halving of current capacity to around 100 kcgrrt, and a reduction of the labour force by around two-thirds to some 7,000, would seem to meet this requirement.

How to set the target

10. The Secretary of State for Trade and Industry considers however that adopting an explicit target at the level of 100 kcgrrt might have major social and political implications, particularly in the North East. He therefore proposes, while endorsing the broad approach of the corporate plan, to point out to BS that EC considerations and public expenditure constraints call for a volume of production below that implied by Option 1. He proposes, principally by setting tough EFLs, to require BS to adopt a target which would be nearer in practice to Option 3, but which:

- i. would seek to operate by controlling order levels, rather than closing physical capacity on a large scale (E(A)(84)43, paragraph 13);
- ii. would not be quantified in its effects on production or employment; and



- iii. would not necessarily imply departure from the BS preferred option of restructuring through "part-closure" rather than the closure of major yards.  
(It would, however, be necessary to sell or close "peripheral" yards at Ailsa and Appledore).

11. This idea has obvious attractions. It could not free the Government from a major share of the responsibility for decisions about capacity and their social, regional and industrial relations effects, but it would maintain pressure on BS to take a full share of the responsibility for such decisions and provide them with a flexible framework in which to exercise their commercial and managerial judgement. The Sub-Committee will also want to satisfy themselves, however, that a restructuring as fundamental as Option 3 could be achieved without major yard closures, in the way described by the Secretary of State; and consider how long it might take to have full effect: there is little detailed information bearing on this in the paper. Also, are Mr Day and the BS Board likely to acquiesce in this approach to the problem?

#### EC implications

12. The Commission have made it clear that they expect "continuing contraction of both employment and capacity" in return for a further deal on IF. Bearing in mind that Mr Tebbit does not envisage the adoption of an explicit target for capacity and manpower reduction, it may not be easy to demonstrate to the Commission that its conditions will be met. If Mr Tebbit's approach is approved, further work will be needed on how best to handle the discussions with the Commission.

Other matters

13. E(A)(84)43 also mentions three further points on which work is in hand.

i. Combined Provision for IF and Soft Credit

Mr Tebbit says in paragraph 14 iii that he is considering an arrangement under which BS, subject to appropriate ground rules, would be left to manage for themselves a total provision to cover both IF and soft credit. A further report is promised. The most obvious effect would be to make it harder for BS to press "ad hoc" for soft credit to top-up IF terms. This ought to enhance somewhat the financial disciplines on the Board. The Sub-Committee will wish to invite Mr Tebbit to report in due course.

ii. Engine-building

The Sub-Committee will wish to note the action already being taken by BS, described in paragraph 18 in E(A)(84)43 and in Annex F, to restructure engine-building capacity on two sites instead of five; and Mr Tebbit's judgement that it will be desirable eventually, on the order books he foresees, to concentrate engine-building in the UK on one site either at Kincaids or Harland and Wolff. A joint paper by the Secretaries of State for Trade and Industry and Ireland is promised in the Autumn (E(A)(84)43, paragraph 18).

iii. Shipbuilding Redundancy Payment Scheme

This statutory scheme runs out in 1985, a time which may be crucial to privatisation. This raises complex technical and legal questions, as well as the broader tactical one of whether it is better to allow the scheme to lapse, taking the chance that the unions will use the imminence of privatisation as a lever in an attempt to extract



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more favourable terms; or whether it would be preferable to reduce uncertainty, which might have an adverse effect on the market, by extending the statutory scheme for one year. BS are preparing an assessment of the options and their effects on privatisation, which the Secretary of State for Trade and Industry proposes to discuss with the Chief Secretary, Treasury when it is ready: no doubt the Sub-Committee will wish to invite them to report when they have considered it.

#### HANDLING

14. You will wish to ask the Secretary of State for Trade and Industry to present his paper. The Secretary of State for Northern Ireland may have comments. The Chief Secretary, Treasury will wish to respond. If the Foreign Secretary or a representative attends, he may have points to make on the progress of negotiations with the EC over IF. The Secretary of State for Defence will attend because of his interest in warshipbuilding and should be given a chance to comment.

#### CONCLUSIONS

15. You will wish to reach conclusions on the following:
- i. whether the capacity of BS for merchant shipbuilding should be allowed to contract over the period to 1987/88 to about 100kcgry;
  - ii. whether targets for the merchant shipbuilding capacity of BS should be set
    - a. explicitly, in terms of capacity and/or employment; or
    - b. implicitly through tough EFLs and other financial disciplines, as proposed by the Secretary of State for Trade and Industry;
  - iii. whether future work on
    - engine-building and
    - the shipbuilding Redundancy Payments Schemeshould proceed as proposed in paras 18-20 of E(A)(84)43.

*PLG*

P L GREGSON

17 July 1984

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JF6969  
Secretary of State for Trade and Industry

16 July 1984

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The Rt Hon Peter Rees QC MP  
Chief Secretary to the Treasury  
HM Treasury  
Parliament Street  
LONDON  
SW1P 3AG

*D Peter,*

BRITISH SHIPBUILDERS' PROSPECTIVE ORDER FOR SMITH'S DOCK  
FROM BUE

Thank you for your letter of 12 July.

2 I remain unconvinced, but in the light of the position you have taken we must cross our fingers and hope that Hamilton does not pull out without at least giving BUE an ultimatum.

3 I am sending a copy of this letter to the Prime Minister, other members of E(NI) and to Alick Buchanan-Smith.

NORMAN TEBBIT

NAT IND

PT 7 Shipbuilding

16 JUL 1984

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Secretary of State for Trade and Industry

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13 July 1984

The Rt Hon Nigel Lawson MP  
Chancellor of the Exchequer  
HM Treasury  
Parliament Street  
LONDON  
SW1P 3AG

D Nigel

BRITISH SHIPBUILDERS' PAY 1984/5

Thank you for your letter of 15 June.

2 I am glad you agree that we should not press BS to go for a lower settlement than 4 per cent. Since writing to you on 8 June I have learned that Harland and Wolff have settled for 6 per cent; against that background any pressure on BS would be almost impossible to sustain.

3 BS opened their pay negotiations on 18 June with an offer worth 3 per cent overall. It was rejected by the unions, who particularly opposed the structure of the offer, designed as I described in my letter of 8 June to enhance differentials. The two sides meet again on 16 July. BS then propose to make their final 4 per cent offer. They expect the detailed negotiations to be difficult but are hoping to reach a settlement that day.

4 I have considered, as you suggested, whether to press BS to make an explicit link between this pay offer and productivity improvements, but have decided that this would not be the best way forward. Last year's £7 pw award was and remains conditional upon the implementation of radical changes in working practices; it can be withdrawn on an individual basis if necessary. What BS seek this year is a short negotiation followed by a period of stability and I think they are right to go for the package as it stands.

5 Nor do I think it would be right to press BS to separate warship and merchant shipbuilding pay negotiations. That would be likely to lead to a higher settlement overall. BS judge that they must give a 4 per cent overall deal to the merchant yards to

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achieve their aims of increasing differentials and avoiding disruption. If the warship yards negotiated separately they would undoubtedly press, on the basis of their profitability, for a much better deal. Moreover an attempt to separate the negotiations would be strongly resisted by the unions and would provide an issue around which the Shipbuilding Negotiating Committee, much weakened by last year's disputes, could cohere. It would in my view be an entirely counter-productive approach.

6 Copies go to the Prime Minister, Jim Prior, George Younger and Tom King.

A handwritten signature in black ink, appearing to read 'Norman Tebbit', written in a cursive style with a long horizontal stroke at the end.

NORMAN TEBBIT

NAT IND: Shipbuilder: Pt 7



13 JUL 1984



NRSM

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Treasury Chambers, Parliament Street, SW1P 3AG

Rt Hon Norman Tebbit MP  
Secretary of State for Trade & Industry  
Department of Trade & Industry  
1 Victoria Street  
LONDON  
SW1E 6RB

12 July 1984

*Norman Tebbit*

**BRITISH SHIPBUILDERS PROSPECTIVE ORDER FOR SMITH'S DOCK FROM BUE**

Thank you for your letter of 6 July asking me to reconsider my position on the BUE order. I have done so carefully in the light of your and Alick Buchanan-Smith's further comments but have to say I remain unconvinced.

The main arguments you use for conceding the subsidy to enable BS to accept this order are, respectively, its importance for the future of BUE and the threat of adverse publicity (from inter alia BUE) if we do not provide the necessary assistance. You do not mention the future of Smith's Dock, which is I believe due to run out of work very shortly, though you do suggest that acceptance of this order should not materially prejudice decisions on the Dock's future, a point which I must say I find it difficult to accept.

There is a serious danger of the tail wagging the dog. BUE is a small company under the control of the BTG. The subsidy you are seeking for this order is, at over £4 million, getting on for 20% of BUE's total turnover. The strategic considerations as regards the future of BS's merchant shipbuilding activity must considerably outweigh the importance of BUE which seems to be primarily concerned to create a UK presence in an area of North Sea activities already well served by the Americans and Dutch.

The subsidy proposed is, at 31 per cent of the cost of the ship, very high. The further £5 million guarantee that BS

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is required to give for four years, (to be extended if the ship's performance or value does not come up to expectations), is one which, to use Norman Lamont's phrase, one must have considerable reservations about. BS had total guarantees outstanding of about £65 million in March 1983 (last published accounts). These will of course become additional public expenditure if the guarantees are called.

I find it very difficult to accept the case for giving this subsidy solely on the basis that it will avoid adverse publicity and not materially prejudice decisions on the future of Smith's Dock. It will surely not be any easier to take difficult decisions on the future of Smith's Dock in April 1985 than it is now, particularly with the workforce dragging their feet on a BUE contract, with high penalties for delay, because it is the last ship in the yard. Nor will adverse publicity be any easier to cope with then than now. (So far as delay is concerned I note Alick Buchanan Smith's statement in his letter of 5 July that BUE submitted their request for financial assistance over 4 months earlier).

For this kind of reason it seems to me that we buy a short breathing space only at the expense of making it more difficult both to formulate and to pursue a sensible strategy for BS's merchant shipbuilding. Even were the terms of the proposed Government assistance for the BUE order acceptable, which in my view they are not, I would wish to argue that our attitude should be based on our overall objectives for the industry and the limited timescale we have for achieving them.

In arguing for a decision on the BUE order to be deferred in my earlier letter, I was seeking to avoid pre-emption of the collective discussion, for which I have been pressing for some months and which has now been arranged for next week, about the strategy for merchant shipbuilding and the linked issue of the degree of subsidy to be provided. This will I hope provide the much-needed policy framework within which to fit our future decisions on subsidy for individual orders. But acceptance of this case now would pre-empt our discussion in the wrong direction. If you believe it is impractical to defer a decision further, then I think the decision should be to reject the order on the grounds that the terms and conditions impose an unacceptable burden, both actual and contingent, on BS and the taxpayer.

I would like to take this opportunity to respond also to Norman Lamont's letter to the Chancellor of 2 July on the prospective order from C Y Tung for Govan shipbuilders. Very similar considerations appear to me to apply here reinforced by the even higher subsidy level of 41 per cent proposed in this instance. I understand that your officials have indicated that a measure of delay would be tolerable and I certainly believe that that is the right course in the circumstances.

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I am sending a copy of this letter to the Prime Minister,  
other members of E(NI) and to Alick Buchanan-Smith.

*Yours truly*  
*Peter Rees*

PETER REES

CONFIDENTIAL

Shipbuilding Pol: NAT. INDS. Pt 7.

11 JUL 1967





JF6930

PS/  
Secretary of State for Trade and Industry

*BIF for FERS at  
business meeting.*

*AT 11/7*

DEPARTMENT OF TRADE AND INDUSTRY

1-19 VICTORIA STREET

LONDON SW1H 0ET

TELEPHONE DIRECT LINE 01-215 5422

SWITCHBOARD 01-215 3422

*ce NO*

11 July 1984

CONFIDENTIAL

R Hatfield Esq  
Private Secretary to  
Sir Robert Armstrong  
Cabinet Office  
Whitehall  
LONDON  
SW1

*Dear Richard,*

PRIVATISATION OF WARSHIPBUILDING

It was agreed at E(A) on 20 June that warshipbuilding privatisation would have to be referred to Cabinet, and that it was desirable that E(A) should have considered beforehand the prospects for British Shipbuilders' merchant shipbuilding capacity.

2 As you will know, my Secretary of State is planning to circulate a paper to E(A) this week on merchant shipbuilding for discussion on 18 July. My purpose in writing is to let you know that he would like warshipbuilding to be discussed in Cabinet on 19 July and that he proposes on Monday, 16 July to circulate a paper on it for Cabinet. He hopes that Sir Robert Armstrong will agree to recommend this course.

3 Ideally, of course, it would have been preferable to have longer between the E(A) discussion and the Cabinet decision on warships. However, my Secretary of State believes it is important for the Government to decide in principle before the Summer break how it wishes to proceed on warship privatisation, to prevent further delays in the timetable. Although the gap between the two discussions will be very short, the link between the issues is political rather than technical. The outcome of the E(A) discussion can be reported orally to Cabinet, and it is clear that any delay of the Cabinet discussion beyond 19 July would, on current timetables, make it very difficult to announce the Government's decision on privatisation of BS' warship yards before Parliament rises. This would clearly be most undesirable.





CONFIDENTIAL

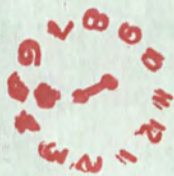
4 I am copying this letter to Andrew Turnbull at No 10 with whom I have discussed the matter, and on whose suggestion I am writing to you.

*Yours sincerely,*

*Ruth Thompson*

RUTH THOMPSON  
Private Secretary

Shipbuilding; NAT. IND. AT.



1984 JUL 7



NBRM  
BT 9/7  
CC 100

SCOTTISH OFFICE  
WHITEHALL, LONDON SW1A 2AU

CONFIDENTIAL

The Rt Hon Nigel Lawson MP  
Chancellor of the Exchequer  
HM Treasury  
Treasury Chambers  
Parliament Street  
LONDON  
SW1P 3AG

6 July 1984

Dear Chancellor,

GOVAN SHIPBUILDERS: PROSPECTIVE ORDER FROM C Y TUNG

I have seen a copy of Norman Lamont's letter of 2 July to you and am writing to strongly support his proposal that Graham Day should be authorised to take the above order on the terms outlined.

Govan has greatly improved its performance in recent years and on any indicator is now one of the best BS yards. It would accordingly be unthinkable in my view not to regard it as a 'core' yard in the Corporation's future strategy for merchant shipbuilding. I therefore hope that the proposal outlined in Norman's letter can be agreed in advance of our consideration of the BS Corporate Plan. Although the level of public support proposed is undoubtedly high, I believe that assistance of this order is necessary if our good yards are to survive in the face of fierce competition from the Far East; indeed that is what our approach to the EC is all about.

I am copying this letter to members of E(A), Geoffrey Howe and Jim Prior.

Yours sincerely

Approved by the Secretary of State  
and signed in his absence

NAT IND PT 7

Shepherdway

19 JUL 1961

11  
1961

CONFIDENTIAL

NBPM 17/17 VENO



DEPARTMENT OF TRADE AND INDUSTRY

1-19 VICTORIA STREET

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Secretary of State for Trade and Industry

6 July 1984

The Rt Hon Nigel Lawson MP  
Chancellor of the Exchequer  
HM Treasury  
Parliament Street  
London SW1

D Nigel,

BRITISH SHIPBUILDERS - PROSPECTIVE ORDER FOR SMITHS DOCK FROM BUE

I would like to echo the concern expressed by Alick Buchanan-Smith in his letter to you of 5 July, and to urge you and Peter Rees to think again about the line we should take on the BUE order.

2 Peter Rees' letter of 29 June suggests that we should defer a decision until we collectively consider BS's Corporate Plan. Other things being equal, that would be a very sensible approach; but other things are not equal, and if we do attempt to delay a decision for another fortnight we face the very real possibility that the order will be lost.

3 In addition to the Energy considerations mentioned by Alick Buchanan-Smith the loss of the order would have two further very serious consequences. First, it would at best delay by upwards of a year, and at worst totally destroy the chances of privatising BUE. Without the Hamilton order it is indeed on the cards that BUE would end up in Receivership. It would be very difficult indeed to explain and defend such an outcome. BUE have told us today that they have felt obliged to defer privatisation for at least two and a half months because of the delay in reaching a decision on the ship order.

4 This brings me to the second point. If the order is lost I have no doubt that there will be virulent adverse publicity for the Government as a whole and for my Department and perhaps yours in particular. BUE are well aware that Treasury Ministers have had the case before them since early in June and where the issue now stands. There is indeed a strong possibility that they will shortly disclose to the press their decision to defer privatisation.

JH3APE



CONFIDENTIAL

5 In the circumstances I believe that the only credible course is to agree now to the proposal set out in my letter to Peter Rees of 8 June. I do not think that acceptance of this order by Smiths Dock would prejudice materially whatever decisions we take on the BS Corporate Plan. The terms of the deal require the vessel to be completed by April 1985 if penalties are to be avoided. Thus it give Smiths Dock only a relatively short breathing space. Moreover, given the stringent delivery date the sooner the order can be begun the better.

6 I very much hope therefore that you and Peter Rees can very rapidly reconsider the Treasury position.

7 I am copying this letter to the Prime Minister, other Members of E(NI), and to Alick Buchanan-Smith.

A handwritten signature in black ink, appearing to read 'Norman Tebbit', with a long horizontal line underneath.

NORMAN TEBBIT

JH3APE

Nat Ind: Shipbuilding Pt 7.

NSM AT 5/2/84

DEPARTMENT OF ENERGY  
THAMES HOUSE SOUTH  
MILLBANK  
LONDON SW1P 4QJ

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THE MINISTER OF STATE

The Rt Hon Nigel Lawson MP  
Chancellor of the Exchequer  
HM Treasury  
Treasury Chambers  
Parliament Street  
LONDON  
SW1P 3AG

5 July 1984

Dear Nigel,

BRITISH UNDERWATER ENGINEERING LIMITED (BUE) - CONSTRUCTION OF  
FIELD SUPPORT VESSEL

I wrote to you on 14 June regarding the above vessel. I have now  
seen a copy of Peter Rees' letter of 29 June to Norman Lamont. I  
am extremely disappointed.


A major order of considerable importance both to BUE and to our  
national interest is now in serious jeopardy. May I repeat again  
the points I made in my own letter to you?

BUE is the only wholly UK underwater engineering company and the state  
owned British Technology Group is its major shareholder. The under-  
water sector of the offshore market has always been of critical  
importance, particularly in export markets and BUE is central to our  
long-term plans. The company, which was set up in 1979, is now  
firmly established although it is still relatively small in a market  
dominated by powerful overseas contractors.

Unlike BUE, most of the major underwater contractors possess a vessel  
from which they can undertake diving services; BUE has to hire boats  
to enable it to carry out this work and its preferred vessels are  
not always available. Furthermore, ready access to a technically  
advanced vessel has become a major consideration for oil companies  
when awarding long term contracts. With some difficulty, Hamilton  
Brothers have been persuaded to offer BUE a four year contract to  
perform diving services for them on the UKCS and this guarantee of  
employment has presented BUE with a unique opportunity to build an  
advanced and highly sophisticated field support vessel. But that  
build cannot now go forward without the Section 10 support and BS  
guarantee for which Norman Lamont's letter sought approval. It is  
ironic that BUE will lose the order because they proposed a British  
Shipyard for the build. Had they gone forward with a foreign build  
the vessel would be half complete by now. I expect other potential  
BS customers will take due note.

I know, of course, that the vessel will contain a number of unproven  
features and that the proposed exposure of public funds in supporting  
the project is not insignificant. However, there is no doubt in my  
mind that the Hamilton contract is vital to BUE if the company is  
to build up its share of the underwater market both on the UKCS and





in the offshore markets world wide. The project will also benefit UK manufacturers and suppliers as the bulk of the high technology equipment will be obtained from UK sources. Moreover two or three other oil companies have expressed an interest in the vessel and this contract is likely therefore to lead to further charters and, by extension, further orders for British Shipbuilders.

BUE submitted the request for financial assistance to the Department of Trade and Industry over four months ago and since 8 June the matter has been under consideration at the Treasury. Peter Rees' letter suggests further delay. Frankly there is no more time. As it is (and four months already an incredibly long time for any commercial decision to be deferred) delivery of the vessel has slipped well beyond the date Hamiltons envisage. Hamiltons have emphasised to us that the delay is interfering with their field development plans and that they cannot long delay placing an alternative order overseas. This decision - which is imminent - would be a real body blow and will certainly not wait upon further consideration of British Shipbuilders' future.

I am continually urging oil companies to co-operate in advancing UK indigenous offshore technology and I am deeply worried that an important project like this should be placed in jeopardy through protracted discussions over the strategic interests of British Shipbuilders. If BUE lose this order the company will immediately lose credibility in the market place and will inevitably go into decline which could end in collapse or its takeover by an underwater engineering company which would almost certainly not be British.

I feel very strongly that an opportunity such as that presented by the Hamilton contract should not be allowed to go by default and that it would not be in the national interest for the project to go abroad. In these circumstances I would be grateful if you could reconsider the matter and agree to support the BUE proposal.

Incidentally, there is a risk of BUE making public that the UK is in danger of losing a valuable contract because of the delay in dealing with their application for support. Such unwelcome publicity would be difficult to counter in an effective way.

I am copying this to the Prime Minister and to other members of E(NI).

*You are*  
*Alic*

ALICK BUCHANAN-SMITH

---

MAT 120: Shipbuilding P27





NAPM  
BT 2/7  
a 10

DEPARTMENT OF TRADE AND INDUSTRY  
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From the Minister of State for Industry

Norman Lamont MP

**CONFIDENTIAL**

Rt Hon Nigel Lawson MP  
Chancellor of the Exchequer  
HM Treasury  
Treasury Chambers  
Parliament Street  
LONDON SW1

2 July 1984

*Dear Nigel*

**GOVAN SHIPBUILDERS - PROSPECTIVE ORDER FROM C Y TUNG**

I have been approached by British Shipbuilders with a request for the provision of an exceptional level of support for a prospective order from C Y Tung for a 61,000 dwt products tanker. The order, at a contract price of £23.3m, would be placed with Govan for delivery in June 1986.

As you know, Govan is one of the yards around which BS hopes to construct its future merchant shipbuilding organisation. The yard has not yet moved out of a loss-making situation, but BS regards both its management and its facilities as very good and thus it is a core yard. Nothing therefore in this letter is likely to preempt anything in the Corporate Plan decision.

The yard is now in the final stages of completing the second of the two ships for Jebsen and has recently been successful in securing the three colliers for the CEBG, which involves no exceptional assistance at all. These will, however, occupy no more than about half of the yard's available resources, even at the peak period of their construction. Thus substantial under-recoveries of overheads are likely to arise during the period until December 1985, when the last of the three ships is due for delivery, unless further orders can be secured. The order now proposed by Tung would provide for the recovery of overheads totalling some £6m during the period of construction of the CEBG ships on the assumption that, as BS intend, the yard is to remain at about its present size.

The financial package proposed by BS for this order, however, does involve both significant subsidy costs and a financial structure which is slightly more hazardous than normal in an international context.

1THAAC



The exceptional subsidy elements proposed for this deal fall into two parts. Intervention Fund has been requested at the rate of 20.4% instead of the normal 15%. BS also proposes to provide for the reduction of the rate at which the ship would be leased (by a UK lessor to a UK member of the Tung group) by undertaking to make a 'balloon' payment totalling 30% of the contract price (£7m) at the end of the 15 year lease period. BS would provide for this 'balloon' payment by buying fixed interest gilts of the appropriate maturity. Assuming an interest rate of 10%, this would mean an investment now of £1.67m or 7.2% of the contract price, which is, in effect, the NPV of this element of the support.

The total costs of the package would therefore be:

	<u>% of Contract Price</u>	<u>£ million</u>
<u>Standard Aids</u>		
Intervention Fund	15.0	3.50
Shipbuilders' Relief	2.0	0.47
Home Credit (NPV)	<u>11.2</u>	<u>2.61</u>
	28.2	6.58
<u>Exceptional Aids</u>		
Additional Intervention Fund	5.4	1.25
Lease Support (NPV)	<u>7.2</u>	<u>1.67</u>
	12.6	2.92
<b>TOTAL</b>	<b>40.8</b>	<b>9.50</b>

I recognise that this proposal does involve a large subsidy element, although it is fair to point out that it is very close to the level which would be involved if Intervention Fund were now available normally at the 30% rate which we have already discussed in the context of our recent proposals to the Commission.

I am also conscious that the provision of Intervention Fund at a higher than normal rate may be open to criticism by the Commission, if it were to be found out. With this in mind, BS have explored the possibility of constructing alternative packages which would not involve more than 15% Intervention Fund. It has not proved possible to construct workable arrangements along these lines other than at significantly greater subsidy costs.

While it would have been preferable to avoid taking the course proposed, had that been possible, I do not think that it involves unacceptable risks. The amount of Intervention Fund above the norm is not very high and it would be extremely difficult for the



Commission to deduce that there had been a breach from the kind of information that normally becomes public about shipbuilding orders. Moreover, we are, as you know, trying to secure the Commission's consent for an IF intensity of 30% and they have given us a hint - though no more than that - that 25% might prove acceptable (against the 20% involved in this case). Finally, we have seen a draft of the Commission's initial response to our notification which says in its closing paragraph that "any aid granted before the Commission had reached its final decision may therefore be subject to a recovery order". This appears to open the way for BS to take the order subject to their being required to refund the subsidy or that part of it which exceeds the level allowed by the Commission.

In considering the scale of the subsidies involved in this proposal, it is also appropriate to bear in mind the recovery of overheads to which I have referred above, which would more than offset the exceptional elements in the proposed subsidy package and, indeed, largely cover the standard Intervention Fund element as well.

Taking all of these considerations together, I believe that this is a proposal which, despite the obvious difficulties, it is right that I should recommend to you. Graham Day is anxious to be in a position to sign a contract quickly and I should therefore be grateful to know as soon as possible whether you are able to agree to my approving the support package which he has requested.

I am copying this letter to other members of E(A), Geoffrey Howe and Jim Prior.

*Yours*  
*N Lamont*

NORMAN LAMONT

CONFIDENTIAL



*cc wj*

*NBRM*

*BT 2/7*

Treasury Chambers, Parliament Street, SW1P 3AG

Norman Lamont Esq MP  
Minister of State for Industry  
Department of Trade & Industry  
1 Victoria Street  
LONDON  
SW1E 6RB

29 June 1984

*Norman*

**BRITISH SHIPBUILDERS - PROSPECTIVE ORDER FOR SMITHS DOCK**

Thank you for your letter of 8 June about the terms requested by British Shipbuilders (BS) for an order for Smith's Dock from BUE Ships Ltd.

I agree with you that the terms proposed are difficult to contemplate and I endorse your reservations about the size of the guarantee. Moreover, despite what you may say about Smith's Dock being a core yard for BS's future strategy there must surely be some doubt as to whether colleagues will be able to endorse this strategy. In view of this and since colleagues will very shortly be considering the future strategy for BS I think we should defer a decision in this case until we can see more clearly how it fits whatever strategy is agreed.

I am sending copies of this letter to members of E(NI) and to Alick Buchanan-Smith.

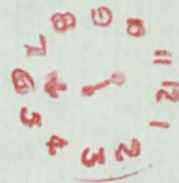
*Norman* *RTW*

PETER REES

CONFIDENTIAL

MATIND PT 7

Shepherdson



- 2 JUL 1984



10 DOWNING STREET

Prime Minister

Mr Tebbit has asked to stay  
behind after E(A) for 10 minutes  
to give you a preview of the  
difficult decisions on shipbuilding.

AT

27/76





## THE BILL

British Shipbuilders, like all nationalised industries, looks to the Treasury for external finance which it usually receives in the form of loans and public dividend capital. Under the 1977 Aircraft and Shipbuilding Industries Act, which created the Corporation, the original limit for this finance was £200 million. This was increased, in stages, to £800 million by July 1983. The British Shipbuilders (Borrowing Powers) Bill was introduced into the House of Commons in November 1983, enabling the Secretary of State to increase this again, initially to £1000 million and eventually, with the further consent of the Treasury and the House, to £1200 million. This Bill puts into effect this further increase in the external financing limit to £1200 million. This is necessary because of British Shipbuilders' continuing difficulties and the lack of any significant upturn of its markets.

## Background

British Shipbuilders was established under the Aircraft and Shipbuilding Industries Act, 1977, after a prolonged Parliamentary struggle. It was formed from twenty-seven companies in shipbuilding, ship repairing and marine engineering.

Shipbuilding in Europe declined throughout the 1950s and 1960s. In the UK the slide has been especially marked. Our share of the world market fell from nearly 40 per cent in 1926 to 20 per cent in 1956 and just 2 per cent today. In the UK, employment in this sector fell from 130,000 in 1955 to 69,000 in 1973. From 1974 the threat of nationalisation hung over the industry, world demand continued to decline and its financial problems continued to be acute.

Since nationalisation, the industry has received over £1,192 million in grants and loans from the Exchequer. If it had remained in the private sector it would have needed assistance, but it would also have faced up to the need for rationalisation much sooner and the cost to the Exchequer might well have been less.

The Government has made it clear its commitment to the industry, but it has also emphasised that the ultimate size and shape of the industry must depend on its competitiveness. Productivity is still below pre-nationalisation levels, so there is considerable room for improvement.

As Mr Norman Tebbit has said:

'We have not, nor will, we shrink from support where it can lead to viability, nor shall we shrink from facing the facts squarely when a yard has no customers willing to place work in it' (Hansard, 1st February 1984, Col. 304).

In 1982-3 British Shipbuilders lost £117.5 million, an increase of 600 per cent and far in excess of its agreed loss limit. The Financial Times reported that British Shipbuilders' losses for the financial year to March 31st 1984 are likely to total at least £150 million, £30 million more than previous estimate' (12th June 1984). Mr Graham Day, Chairman of British Shipbuilders has said that the Corporation's losses in 1984-5 would be much smaller as the effect from the sale of the loss-making Scott-Lithgow is felt,

## Prospects

### Market Situation

Present prospects are still gloomy. The world's shipyards have been badly hit by the recession because their customers, the ship-owners are facing a glut in capacity brought about by the drop in world trade.

In April 1984 there was 77 million deadweight tonnes of idle merchant shipping around the world, an improvement on the peak of 100.5 million dwt in May 1983, but considerably higher than the 59.3 mdwt in June 1982.

### IDLE MERCHANT SHIPPING TONNAGE

	(MDWT)		
	Dry Cargo	Tankers	Total
June 1982	6.5	52.8	59.3
December 1982	23.6	60.1	83.7
June 1983	25.0	72.9	97.9
December 1983	23.0	56.8	79.8
April 1984	18.8	58.2	77.0

(Source: General Council of British Shipping)

The April figure represents 1566 ships or 11 per cent of the total world tonnage; 19 per cent of the world tanker fleet is currently idle. The Annual Report of Lloyds' Register for 1983 reported for the first time since the Second World War, a decline in the world fleet. In 1974 world order books stood at 133 million gross tonnes; by the end of 1983 this was down to only 33 million gross tonnes.

### New Orders

Competition from foreign, mainly Far Eastern, yards is intense. British Shipbuilders' current order book by April 1984 was £2222 million, which includes a merchant shipbuilding order book of £462 million or 28 ships totalling 314,000 compensated gross registered tonnes and £1760 million for 28 warships. This compares with a total order book of £2500 million at November 1983. (NB: The value of order book can vary considerably over a short period of time as new contracts are won and vessels are completed).

### Reorganisation

In March 1984 British Shipbuilders announced major changes in organisation as part of its attempt to curb heavy losses and win much needed orders. The Corporation will operate with only two divisions instead of five. Since April there has been a division combining merchant yards and composite yards. The warship division remains intact prior to privatisation (see below).

In addition it is cutting back its Newcastle-upon-Tyne headquarters by 20 per cent; the savings of £1.5 million will be reallocated to product development.

### Merchant and Composite Yards

This market is very depressed and is not expected to improve significantly over the short term. The merchant yards are most affected by foreign competition.

**Govan Shipbuilders** have, however, recently successfully won orders in/ the face of severe foreign competition. In March they won an order worth £28 million for three colliers from the Central Electricity Generating Board. As Mr Allan Stewart, Scottish Office Minister has said: 'Govan has demonstrated that with the right commitment and working practises British yards can compete in the face of intense competition' (Shipbuilding News, April 1984).

In addition **Govan** has received a letter of intent from the C H Tung Group, Hong Kong for a 66,000 tonne bulk carrier which could be worth over £20 million. Work is also being sought in Hong Kong for **Austin & Pickersgill**. Of the composite yards, **Cammel Laird** failed to win a £111 million oil rig order from Sun Oil in March, and the Unions were recently told that there would have to be 870 redundancies at the yard.

### The Introduction of Private Capital

The Government is committed to the promotion of private ownership in the shipbuilding industry. Under the British Shipbuilders Act 1983 the statutory obstacles to the introduction of private capital have been removed, and provided the Secretary of State for Trade and Industry with enabling powers to direct British Shipbuilders to dispose of particular assets or subsidiaries. BS is now no longer obliged to carry on the full range of activities specified in the 1977 Act that nationalised it; it can discontinue unprofitable work and dispose of profitable yards when appropriate. The Act gives the Secretary of State powers to restrict foreign shareholders in any yards that are sold, and gives him other powers to safeguard assets or activities which are important to our national security. Before giving any general direction to BS the Act also requires that the Secretary of State must be satisfied that it will further the national interest. The recent sale of Scott Lithgow, certain repair yards, and the Government's announced plans to seek private investment for the warship yards, are a result of this Act.

Scott-Lithgow. In March 1984 the Government found a buyer for BSs' biggest loss-maker, Scott-Lithgow. The deal, under which Trafalgar House agreed to continue offshore rig construction at the Greenock yard, has saved approximately 2000 jobs.

As Mr Norman Lamont has said:

'We said that we would not be prepared, with a yard with such a damaging record of huge losses, to go on pouring in taxpayers' money; we had come to the end of the road. Despite not having to put in more money, we have managed to salvage something out of the wreckage and to create an entity that will, we believe, be a strong company in the offshore industry' (Hansard, 28th March 1984, Col. 293).

### Ship Repairing

The slump in world shipping has hit the ship repair yards hard. British Shipbuilders has been gradually moving out of ship repairing. **Redheads**, on the Tyne has been bought by its workforce, whom BS had made redundant. Successful management buy-outs have been achieved at **Tyne Shiprepair** and **Grangemouth Dockyards Ltd.** Taken together these developments have preserved 600 jobs. By March 1984 **Tyne Shiprepair** had booked work for 27 ships worth around £3 million; 4 weeks after it became a private company.

Warship Yards - These yards taken together employ over 20,000 people.

**Vickers, Vosper Thornycroft** and **Yarrows** have a consistent track record of profitability. At April 1984 their combined order book stood at £1760 million. The Navy announced earlier this year that it will be ordering 12 of the new Type 23 frigates, designed by **Yarrows**, over the next decade at the cost of approximately £100 million each. In its 1983 Manifesto the Government said it would return parts of BS to the private sector. In view of the impending privatisation of the warshipbuilding yards the Government has set them a separate External Financing Limit of £80 million for 1984-5. The warship yards made a profit of £54.75 million in 1982-3.

### The 1977 Compensation Terms

While in Opposition, Conservatives strongly criticised the terms of the Nationalisation Bill before its enactment. Total compensation paid for the 24 private companies vested in BS was £75.5 million.

After the 1979 General Election the Government explored every option to see if there was an acceptable and fair way of overriding the terms of the legislation.

It was reluctantly concluded that this could not be done; it would have been wrong to amend the terms now because people have sold shares on the basis of the 1977 Act.

Many of the companies involved have decided to settle for the compensation received, but some of the previous owners brought seven cases against the Government, concerning the amounts they received, before the European Commission of Human Rights. In March the Commission rejected claims that the compensation paid had violated the European Convention of Human Rights, but the cases have now been referred to the European Court of Human Rights for a final ruling.

## BS's Manpower and Finance

### Manpower

BS's work force has been reduced from 87,500 at nationalisation in 1977 to 48,550 by the end of March 1984. In the course of the financial year 1983-4 nearly 14,000 were shed as part of the Corporation's survival plan; this decline however does include a fall of 2,900 employees as a result of the Scott-Lithgow sale. A number of yards were closed in January as part of the continuing rationalisation of the Corporation's activities; these included **Henry Robb** at Leith (383 jobs), **Goole** on Humberside (365 jobs) and **Clellands** at Wallsend (400 jobs) - none of these yards had had any new work since Christmas.

### Finances

British Shipbuilders, like all nationalised industries looks to the Treasury for external finance which it usually receives in the form of loans and public dividend capital. Under this Government BS has received £1094 million in public support broken down as follows:

£782 million in public dividend capital  
£201 million from the intervention fund  
£111 million in special redundancy payments

### **External Financing Limit (EFL)**

The original EFL for 1983-4 of £158 million was re-set at a record £268 million; of the increase £88 million was to cover the costs of disposal of Scott-Lithgow while £22 million was to meet the effects of the continuing world recession in merchant shipbuilding.

Due to the reorganisation of British shipbuilders into two divisions, and the impending privatisation of the warshipbuilding yards, the Government has set a separate limit for the Warshipbuilding Division in 1984-5. The total limit will be £217 million, £80 million for warshipbuilding and £137 million for the rest of the Corporation. The latest British Shipbuilders' Corporate Plan has yet to be made public, but there has been a certain amount of speculation as to the future trend in the Corporation's financing. The Guardian has reported that 'The Corporate Plan envisages that the state company's external financing limits will fall by over £100 million to £115 million in the next financial year (1985-6) and down to as little as £60 million in 1986-7' (11th June 1984).

### **The Intervention Fund**

Exists to help BS compete with cheap Far Eastern prices. The most notable example of its use was when the Government provided around £10 million in order to ensure that **Cunard** built the replacement for the Atlantic Conveyor, lost in the Falklands, at **Swan Hunter** instead of at **Hyundai** in Korea.

The Korean's had quoted £30 million against BS's £40 million and the Korean price was estimated to be the same as BS's material costs alone. BS estimate that approximately 60 per cent of the cost of a ship is accounted for by outside contractors and suppliers, so the benefits of intervention fund spending are spread widely

throughout the economy.

As Mr Norman Lamont has recently said:

'Following consultation with British Shipbuilders we have tabled proposals to the European Commission for a significant increase in the permissible level of Government support for shipbuilding orders. The need to bridge the gap between United Kingdom costs and Far Eastern prices is one of the main reasons for this initiative' (Hansard, 18th May 1984, Col. 286).

**Shipbuilding Redundancy Payments Scheme:** This was introduced in 1978, the present Government extended it in July 1982 so that it will run until 30th June 1985. It was also improved to give more help to those under 40. The savings in manpower were estimated at that stage to be £150 million. So far over 30,000 employees have benefited from it to the tune of £116 million.

£m	1978	1979	1980	1981	1982	1983	1984
Feb to April	-	4.7	15.5	20.1	14.4	28.0	34.0

### World Comparisons

The shipbuilding industry has been faced with severe difficulties throughout the world, not just in the UK. Competition in world markets is severe at a time when world shipbuilding capacity is reckoned to be 40 per cent greater than is required. Some estimates have suggested that Far Eastern prices are at least 30 per cent below those in Europe.

Japan. The total order book increased to 14 million gross tonnes which represents over 40 per cent of the world order book. However, this follows a fall of 35 per cent in 1982 of world forward orders over 1981. However, the shipbuilding division of the large Hitachi Zosen combine reported that their six yards were working at barely 60 per cent of capacity (Sunday Times, 11th March 1984).

Korea. The South Korean industry is now second only to Japan, in 1974 it ranked 70th in the world. Last year it increased its share of the world order book from 9 per cent to 14 per cent. It is often blamed by its Western competitors for unfair competition. The Seoul Government is accused of granting excessive subsidies and export credits to enable its yards to quote prices up to 35 per cent cheaper than its European rivals. The Koreans however claim that their two largest yards, Daewoo and Hyundai, receive no direct Government subsidy - though they did benefit from an initial five-year export credit, but the terms are said to be less favourable than the Japanese offer. Korean yards say they are cheaper because their yards are more modern and efficient, because their raw materials, particularly steel, are cheaper than in Europe, and because they have a cheap and disciplined workforce. The average working week in Korean shipyards is 60 hours and wages are about one-third those paid in Japan.

Sweden. In 1975 its yards employed 28,000 building ships. By 1983 the figure was under 8,000. The Kockums yard is an example where severe restructuring has turned consistent loss-making into a small profit in 1982. The Annual Report of Lloyds' Register for 1983 noted that 'Following dramatic adjustments to Swedish shipbuilding capacity in recent years the future looks more encouraging'.

West Germany. New orders received in 1983 dropped from 4.4 per cent of the world's new orders, to 2.4 per cent. HDW has been forced to close its merchant shipbuilding capacity in Hamburg, while A G Weser, part of the Krupp Group, recently closed its large yard in Bremen with the loss of 2,000 jobs (Financial Times, 14th March 1984).

France. Their order book fell by 31 per cent in 1983. A plan to reduce capacity by 30 per cent over 3 years was announced earlier this year involving the loss of 5,000 jobs out of an industry employing 22,000.

VOLUME OF SHIPBUILDING WORK

(m gross registered tons)

	Completions			End-year order total		
	1973	1982	1983	1973	1982	1983
Japan	14.7	6.7	6.7	59.6	10.1	14.0
S Korea	0.01	1.4	1.5	1.3	2.6	4.6
W Europe	12.0	3.8	4.1	54.9	7.7	5.7
inc Sweden	2.3	0.3	0.3	10.7	0.6	0.5
W Germany	1.9	0.6	0.8	7.3	0.9	0.6
UK	1.1	0.4	0.5	7.5	1.0	0.6
Spain	1.3	0.6	0.5	7.2	1.5	1.2
France	1.2	0.3	0.3	5.2	0.7	0.5
World Total	30.4	16.7	15.7	128.9	29.2	32.6

Source: Lloyd's Register of Shipping - quoted in Financial Times 16th March 1984

Conservative Research Department  
32 Smith Square LONDON SW1P 3HH

AD/CR  
25.6.84

/Annex I...



Direct Aid to Shipbuilding	Home Credit Scheme Aid to Shipowners
<u>United Kingdom</u>	Home Credit Scheme 80 per cent over 8½ years at 7½ per cent. (On orders placed in United Kingdom yards only)
Up to 17 per cent of contract price (Includes 2 per cent Shipbuilders Relief)	
<u>Belgium</u>	Home Credit Scheme 70 per cent over 15 years. Interest relief subsidy (maximum 3 percentage points)
Nil	
<u>Denmark</u>	Home Credit Scheme 80 per cent over 12 years at 8 per cent interest including 2 year grace period
Nil	
<u>France</u>	Home Credit Scheme 80 per cent over 8½ years at 7½ per cent interest.
Up to 20 per cent of contract price (Excludes cost escalation insurance which benefit ranges from zero to 3 percentage points)	
<u>Germany</u>	12½% investment grant. Interest subsidy 1½% (1983) and 2.5% (1984 & 1985). The Investment Grant automatically reduces the amount of credit to which the Interest Subsidy applies). Credit Guarantees at OECD terms.
Nil	
<u>Ireland</u>	Home Credit Scheme 80% over 8½ years at 7½% interest.
Old scheme expired 31 December 1980. No new formal scheme. Subsidy applications considered on a case by case basis subject to EEC approval.	
<u>Italy</u>	1983 Interest relief scheme:- 2.75% of contract price paid six monthly for 12 years.
Wef 1 January 1983 up to 21% of contract price. (In Mezzogiorno maximum is 25%).	
<u>Netherlands</u>	2% Interest subsidy. New investment subsidy of 12%, plus 2.3% premium for 5 years.
1983/84 up to 8% of contract price. Special maxima of 15% (1983) and 14% (1984) for yards in IEC and VCM groups.	
<u>Finland</u>	Home Credit Scheme 80 per cent over period of construction (at least 2 years, normally not more than 8 years) at 11 per cent interest
Nil	
<u>Japan</u>	Home Credit Scheme*. Government (Japanese Development Bank) loan of 50 or 60 per cent, Over 13 years at 7% per cent interest including 3 year grace period. Further
Nil	

Direct Aid to Shipbuilding	Home Credit Scheme Aid to Shipowners
<p><u>Norway</u></p> <p>For cash contracts subsidies given in 5 annual instalments to a total value of the amount that would have been given on the same contract under home shipowners finance scheme.</p> <p><u>Spain</u></p> <p>Up to 9½ per cent of contract price.</p> <p><u>Sweden</u></p> <p>For 1984 and 1985 a total of £40m budgetted for Government write-off loans to shipyards.</p>	<p>loan available from commercial banks, acting in conjunction with JDB, for 15 or 20 per cent of contract over 8 years at 8½ per cent interest. Supplementary provision in certain cases for interest subsidies of 2½ per cent to 3½ per cent.</p> <p>80% of contract price over 8½ years at 8% interest. The scheme also applies to longer or shorter term financing, but always contains the same amount of subsidy; in the case of cash payment the subsidy is equal to that of a 5 year loan.</p> <p>Home Credit Scheme. 85 per cent over 12 years at 8 per cent interest with up to 2 years grace period. (Smaller subsidy - 60 per cent of value at 8 per cent for 5 years plus 1 year grace - available for conversions and major repair work).</p> <p>Credit Guarantees of 90% of contract price for up to 12 years on commercial loans. Interest rate subsidy about 2½% available in certain cases.</p>

Notes

\* Japanese Home Credit. The 60% and 20% loans are available only for LNG carriers. Other types of vessel attract the lower percentages.

ccno  
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SECRETARY OF STATE  
FOR  
NORTHERN IRELAND  
The Rt Hon Nigel Lawson MP  
Treasury Chambers  
Parliament Street  
LONDON SW1

NBM  
Dr.

21 June 1984

*Nigel*

BRITISH SHIPBUILDERS PAY 1984/85

Norman Tebbit has copied to me his letter of <sup>8</sup>7 June concerning the British Shipbuilders (BS) 1984/85 wage negotiations. I have also seen your letter of 15 June in reply.

It was helpful to have the thinking behind the Corporation's proposals set out in some detail. Clearly there is a considerable element of judgement involved, given the complexities of the achievements that are being consolidated. I agree that it makes commercial sense to consider the wider interest of BS and that the wage round for this year should not be treated in isolation from the previous year's settlement. Accordingly I would not dissent from Norman's view that he should not seek to dissuade BS from making the proposed offer.

Copies of this letter go to the Prime Minister, Norman Tebbit, George Younger and Tom King.

*Younger*  
*King*

CONFIDENTIAL

Nat Ind Shipbuilding

Pt 7



MO 26/3/1

PRIME MINISTER

WARSHIPBUILDING PRIVATISATION

We are to discuss Norman Tebbit's further paper on this subject (E(A) (84)32) on 20th June. Colleagues may find it helpful to have my views in writing beforehand (since, as the Chief Secretary, Treasury has already indicated, no time was allowed for effective consultation - even at official level - before the paper was circulated). I have also had the opportunity to discuss these matters further with Graham Day.

2. The first point to be made is that the statement of British Shipbuilders' views attached to the paper was out of date by the time it was circulated in that by then the Cammell Laird work force had signed the agreement on improved working practices and productivity, and accepted selective compulsory redundancy. Thus, the major precondition of what BS refer to as their alternative strategy has been met, and with this one of the principal uncertainties before us at the earlier meeting of E(A) has been cleared up. The remaining elements of the survival strategy for Cammell Laird (Annex B to E(A) (84)32) are matters for Government and the management of British Shipbuilders.

3. Secondly, I note that BS at least do not consider that the retention of capacity at Cammell Laird would severely reduce the prospects for privatisation. This view should encourage us not to regard the reduction of capacity as an essential prerequisite of successful privatisation. Apart possibly from Vosper Thornycroft's steel yard at Woolston (if it does not succeed in winning a frigate order from Pakistan) Cammell Laird is the only yard which is a



candidate for closure in the timescale for privatisation. This indicates that we could achieve the objective of privatisation while avoiding the odium which will attend what will be seen as a Government-inspired closure of Cammell Laird.

4. Thirdly, I note also that, whilst BS consider that the proceeds from privatisation would be reduced if Cammell Laird were retained, no estimate of this is now before us. As Norman Tebbit said in his earlier paper no estimate of the likely proceeds of any disposal route is robust enough to be offered with any confidence. What is quite clear, however, is that substantial costs to the Exchequer would flow from the closure of Cammell Laird and the general increase in local unemployment which would follow. I do not believe that we should attach significance to a potential and unquantifiable loss of proceeds in the absence of a wider economic assessment of the costs and benefits of closure. I had believed that a significant reason to delay a decision at our earlier meeting was to provide a proper assessment of all the costs of the choices before us. But this has not happened.

5. These factors taken together suggest that the balance of considerations affecting the future of Cammell Laird point much more clearly to the adoption of the alternative strategy set out in British Shipbuilders' note. I fear that we should be deluding ourselves if we took the view, expressed in paragraph 6 of the paper, that the difficulties of closure may not be as great as we had feared. It was made very clear recently to one of my Ministers by a delegation from the Trades Unions at Cammell Laird, in the presence of the local MPs, that the workforce had done all it could to deliver its side of the bargain and the yard's future was entirely at the mercy of the Government. Indeed Graham Day told me last week that then he would not agree to Vospers retendering as I describe later.

6. In my discussion with Mr Day he emphasised that Cammells was not just a local problem. The ramifications of a closure would spread across the industry. A number of issues are currently in play with



the unions including the disposal of ship-fitting and ship-repair capacity, privatisation, the latest pay offer and the productivity agreements. I believe that Mr Day realises that the resolution of these difficult issues would be made harder. There are issues which might unravel the whole process and the closure of Cammell Laird is one of these. A crisis in the industry would not be helpful to our privatisation plans particularly if it were perceived that the crisis had been precipitated by decisions that could have been avoided.

6. It is relevant to our consideration of the Type 22 orders that, if we decided to invite the three yards to re-tender, Graham Day would instruct Vosper Thornycroft not to submit a bid unless they had first signed the productivity agreement. Cammells have done this. As of the end of last week Vospers had not. He has also told me that the task of building a Type 22 frigate is at the margin of that yard's capabilities, and that the yard would probably be more difficult to privatise with such an order than without. I do not entirely accept these points although the earlier tendering round showed that Vospers could not meet our delivery requirements for both frigates. In any event, we must hope that Vospers are successful in their bid to export 2 Type 21 frigates to Pakistan, the prospects for which remain good. (Vospers have built several Type 21s for the Royal Navy).

7. Lastly, on the issue of capacity, I do believe that Norman Tebbit is underplaying the potential significance of exports. We should not forget that as recently as 1970 there was more warship and conventional submarine construction work being undertaken in this country for export than for the Royal Navy. The warship export market is difficult and erratic but there are already signs of an upturn and, in the Type 23, we shall have a ship which is cheaper than the current generation of frigates and with greater sales potential. We should take care not to prune capacity to the point where such work could not be taken on.

8. There are other issues, on the approach to privatisation which we shall be discussing in E(A). But I very much hope that we shall reach



agreement to place the first of the Type 22 orders with Cammell Laird. This ship will be the final replacement for the four major warships lost in the Falklands and it is particularly important therefore that a decision on the order suffers no further delay.

9. Finally I wish to report to colleagues my own position in this matter in the context of the responsibilities I had for Merseyside. As Secretary of State for the Department of Environment I pressed the social case for placing an order with Cammells. No one could have expected me to do less. In the event John Nott was not able for commercial reasons to do so. I respected that position. But he gave the clearest commitment that Cammells and Vospers would be able to compete for the remaining Type 22 order.

10. I became Secretary of State for Defence. Although I agreed from the defence budget to add a further frigate to the total bringing the competition to two at no stage and in no way did I seek to influence the outcome of the competition between the three British Shipbuilders yards. In these circumstances not only did Cammells win the competition but they won it twice. At that stage I believed it wrong to go through a third process particularly as by this stage the issue of privatisation had entered the list of factors to be taken into account in the award of the contract. It would be indefensible if it were to be felt that in the context of capacity rationalisation as a part of a process of privatisation an area of great social deprivation had been deprived of work which it could claim to have won not once but twice in open competition.

11. I am sending copies of this minute to our E(A) colleagues and Sir Robert Armstrong.

Ministry of Defence

19th June 1984





10 DOWNING STREET

Prime Minister

- (i) Do you want to take Warshipbuilding first? It is both more urgent and more contentious than Wage Controls.
- (ii) Mr Heselgrave and Mr Tebbit have both circulated minutes today. These are in the folder. In addition to reading these, I think you have still to read E(A)(84)32.

AT

19/6



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Secretary of State for Trade and Industry

19 June 1984

CONFIDENTIAL and  
COMMERCIAL IN CONFIDENCE

Andrew Turnbull Esq  
Private Secretary to the  
Prime Minister  
10 Downing Street  
LONDON  
SW1

*Dear Andrew,*

WARSHIPBUILDING PRIVATIZATION : E(A), 20 JUNE

My Secretary of State has just seen a copy of the Secretary of State for Defence's minute of 19 June to the Prime Minister on the above. He has asked me to say that, in the light of some of the views ascribed to Graham Day in the Defence Secretary's minute, he believes colleagues might find it useful to have sight of a copy of a letter he has received from Mr Day, which he had not originally proposed to circulate.

2 I am sending a copy of this letter, and enclosures, to the Private Secretaries of the members of E(A) and to Richard Hatfield in Sir Robert Armstrong's Office.

*Yours ever,*

RUTH THOMPSON  
Private Secretary

JH1ALC

197 Knightsbridge  
London England SW7 1RB  
Telephone: 01-581 1393  
Telex: 8814702 BSBLDR G

jgd/mw/0618/6  
18 June 1984

Rt. Hon. Norman Tebbit, MP,  
Secretary of State,  
Department of Trade & Industry,  
1 Victoria Street,  
London SW1.

*Dear Secretary of State*

During a meeting of the National Defence Industries Council last Thursday afternoon I was asked to speak with Mr. Heseltine following the meeting. On Friday morning I had a scheduled meeting with the Controller of the Navy to discuss areas of disagreement between British Shipbuilders' subsidiaries and MOD. Mr. Heseltine wished to discuss the Cammell Laird situation and the Controller added Cammell Laird as a first agenda item.

The Ministry of Defence is British Shipbuilders' largest customer and as such regular communication is important.

I believe Mr. Heseltine considers that the format of the paper setting out British Shipbuilders' agreed position emphasises the excess capacity issue rather than Cammell Laird. I told Mr. Heseltine that the paper accurately represents British Shipbuilders' views in response to issues we were asked to address. I assured him that these views were strictly commercial and were not the result of any external pressure.

The Controller of the Navy sought to agree the basis for the negotiation of contracts for two Type 22 frigates to be placed with Cammell Laird. I told him that British Shipbuilders were not prepared to let Cammell Laird accept any order unless the outstanding industrial relations issues are resolved as previously detailed. Cammell Laird would also require a non-competitive negotiated contract for the conversion of the "Balder London" to provide fairly immediate workload and help bridge the gap in workload prior to work starting on any Type 22 order. If Ministers were to decide collectively that the Type 22 orders were to be placed with Cammell Laird, we could agree that the most recent lapsed tender could form a basis for negotiation, subject to a number of difficult contractual points being agreed between BS and MOD.

- 2 -

I am concerned that no interpretation of the British Shipbuilders' position be advanced other than as set out in the agreed paper. My primary concern is that there should now be an early decision on this issue. I believe that BS's position is fully and clearly set out. Should, however, further clarification be required, I hope I may continue to furnish it to you personally and directly.

*Yours sincerely*  
*Blake*

J. GRAHAM DAY

*Copy sent to Sys Defence by BS.*

MR. TURNBULL

cc Mr. Redwood

WARSHIPBUILDING PRIVATISATION - E(A) on 20 JUNE

We must get the horse and cart in the right order here.  
The first priority is to decide the shape of a viable  
warshipbuilding industry, fit for privatisation. That  
requires considerable capacity reduction. The future of  
Cammell Laird is a subsidiary part of that.

British Shipbuilders' preferred strategy is to take out  
surplus capacity by closing Cammell Laird altogether, and by  
drastically slimming Swan Hunter and Vosper Thornycroft.  
This will make for the following privatisation package:

Vickers	- submarines
Yarrow	- frigates, destroyers, corvettes and Glass Reinforced Plastic (GRP) vessels
Swan Hunter	- frigates, destroyers and corvettes
Vosper Thornycroft	- GRP vessels only

We support BS' proposal. It brings capacity closely into  
line with predicted demand. It leaves MOD(N) with genuine  
competition for all fighting vessel types except submarines,  
where our requirements are too few to support more than one  
yard. And it leaves no subsidised state yard in a  
position to compete with the privatised yards.

/We urge against

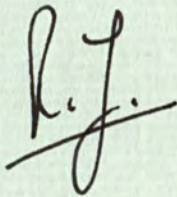
E. R.  
SECRET

-2-

We urge against destroying all this by artificially keeping  
Cammell Laird alive. If Cammell Laird were not on  
Merseyside we would not even be considering it. The  
Government is taking a firm, logical line on the problems of  
Merseyside. If Cammell Laird is closed, that will cause no  
surprise and will soon be forgotten. If the yard is kept  
alive this time, not only will this Government get no credit  
for so doing, but it will have to go on making gesture after  
gesture after gesture. It is not even worth risking an  
invitation to Cammell Laird to tender for the Type 22  
frigates.

In summary, we support all Mr. Tebbit's recommendations  
except the first. If BS' commercial judgement is to  
confine frigate building to Yarrow and Swan Hunter, that is  
where the orders should go.

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BOB YOUNG

18 June 1984



CONFIDENTIAL

P.01317

PRIME MINISTER

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Warship Building: E(A)(84)23, 24 and 32

BACKGROUND

FLAG A  
— The Sub-Committee began their discussion of this subject at their meeting on 10 May (E(A)(84)11th Meeting). As you will recall, the Secretary of State for Defence and the Secretary of State for Trade and Industry gave rather different accounts of the views of the Chairman of British Shipbuilders (BS), Mr Graham Day, regarding the future of Cammell Laird (CL) and warship building capacity. The Sub-Committee concluded that they could not reach decisions on the basis of the information available to them. They invited the Secretary of State for Trade and Industry to obtain from Mr Day fuller and clearer information, including a statement of BS's preferred strategy for warship building capacity, the place for CL in that strategy, and the consequences for other warship building yards if CL were retained.

FLAG B .  
— 2. The latest memorandum by the Secretary of State for Trade and Industry (E(A)(84)32) fulfills this remit. We understand that it has been agreed with the Secretary of State for Defence and the Chief Secretary, Treasury. The memorandum does not, however, appear to change the decisions which Ministers need to take or to require any substantial revision of the brief which I submitted for the meeting on 10 May; for convenience, I attach a further copy. The present minute is simply supplementary comment on E(A)(84)32.

FLAG C  
— 3. Essentially, the BS position as described in E(A)(84)32 is as follows.

Annexes A & B

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(a) If CL could be closed painlessly, BS would do it.

(b) But to close CL without appearing to give the yard a fair trial would have such serious consequences in terms of industrial relations that BS think it must be ruled out.

(c) BS therefore propose to give CL a fair trial, on the basis outlined in Annex B to E(A)(84)32. This is much as previously described to the Sub-Committee. It involves, in particular, directing that at least one of the impending Type 22 frigate orders should go to CL.

(d) If CL failed at this trial BS would close the yard in the expectation of being able to avoid or reduce the consequent trouble with their work-force.

(e) If CL succeeded, then at least BS would have a better shipyard. The problem of over-capacity in warship building would remain; and BS admit that they have no ready solution to this problem. They would have to rely on export orders, sale of the yard to a private sector or overseas buyer, or something else turning up.

4. We understand that Mr Tebbit and his officials remain sceptical about all this, and in particular about point (e). Mr Tebbit appears to accept the BS analysis insofar as he does not propose the immediate closure of CL. But he proposes that the order for Type 22 frigates should be on the basis of competitive tender; no order would be directed without competition to CL. This does not meet the relevant BS condition as set out in Annex B to E(A)(84)32; and it is possible that BS might use this as a pretext for closing the yard and seeking to put the blame on the Government.




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If so, I understand that Mr Tebbit would propose to rely on the following arguments.

(a) If BS do not believe that CL can survive except on the basis of non-competitive orders, the yard does not deserve to survive.

(b) Particularly in view of the almost certain over-capacity in warship building it would be grossly unfair to other yards (particularly Vosper and Swan Hunter, the other runners in the competition for the Type 22 order) to give CL preference.

5. I understand that Treasury officials are briefing their Ministers in similar terms.

  
P L GREGSON  
Cabinet Office.

18 June 1984

Attachment:



NBPM

AT

19/6

Treasury Chambers, Parliament Street, SW1P 3AG  
01-233 3000 15 June 1984

The Rt. Hon. Norman Tebbit MP  
Secretary of State for Trade and Industry

*John Norman*

**BRITISH SHIPBUILDERS' PAY, 1984-85**

You wrote to Peter Rees on 8 June about British Shipbuilders' pay negotiations.

There are certainly arguments for a smaller increase than BS management propose - BS' past and prospective losses; the fact that a pay increase has been paid very recently and the need for further productivity improvements. But in all the circumstances, I accept your judgement that it would not be realistic to press for a lower ceiling. I therefore agree with management's negotiating aim, on the clear understanding that 4 per cent is the upper limit. However, you might like to consider whether they should seek as a further negotiating aim an explicit link with progress on productivity improvements.

I find it disappointing and a little surprising that BS management seem to be reverting to a global pay negotiation for their whole workforce. The warship yards in many respects already constitute a separate business which is profitable and intended for privatisation. In contrast, the rest of BS business is unprofitable and contracting. Would it not make sense for the pay negotiations for these two elements to be conducted separately? There could, of course, be no question of increasing the ceiling for the cost to BS as a whole. But such tactics might help to reduce the extent of industrial trouble.

Copies of this letter go to the Prime Minister, Jim Prior, George Younger and Tom King.

NIGEL LAWSON

*John Norman*  
*Nigel Lawson*

JUN 1984

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BF into Treasury  
response  
AT 816  
CC NO

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From the Minister of State for Industry

NORMAN LAMONT MP

**CONFIDENTIAL**

The Rt Hon Nigel Lawson MP  
Chancellor of the Exchequer  
HM Treasury  
Treasury Chambers  
Parliament Street  
LONDON  
SW1P 3AG

8 June 1984

*Dear Nigel*

**SMITHS DOCK - PROSPECTIVE ORDER FOR BUE SHIPS LTD**

BUE Ships Ltd is a wholly-owned subsidiary of British Underwater Engineering Ltd (BUE), which is, in turn, 67.2% owned by the British Technology Group (BTG). BTG is required under its statutory guidelines to dispose of BUE as soon as commercially practicable. The first step in this process will be the sale of 19% of its share to the other major shareholder, North Sea Assets Ltd, who at present own 17.2% of the company. This will be followed by a share placement expected to raise £6-7.5 million to create about 50% of new equity in the company. The diluted BTG holding would then eventually be disposed of when the company's prospects have improved sufficiently to attract buyers.

These developments are, however, conditional upon BUE Ships having first entered into a vessel charter contract from Hamilton Brothers which has been procured for them with the assistance of the Department of Energy. Without this contract, the company's long term future, and hence its saleability to the private sector, must be in doubt. This contract, in turn, depends upon BUE Ships having concluded a proposed contract with Smiths Dock for the construction of the vessel with which it will meet the charter, at a price of £13.4 million.

Smiths Dock is one of the yards which BS has identified as a core yard for its future strategy. It sees it as meeting an important market sector between the capabilities of its large and small yards. The yard has a good recent financial performance, having reduced a £10 million trading loss in



1979/80 to a roughly breakeven position in both 1982/83 and 1983/84. It has, however, a current order book which runs out in August/September of this year. The survival of the yard depends critically, therefore, on securing new orders virtually immediately. There are no order prospects, other than that from BUE Ships, which are sufficiently firm or far advanced to meet this. Graham Day is keen to secure the order.

Unfortunately, the BUE Ships order can only be obtained on terms which are, in some respects, rather difficult to contemplate. BUE require, in order to make the Hamilton contract viable and to match the financial terms on which their competitors' North Sea operations are based, credit exceeding that normally available under the Home Credit Scheme. The normal credit terms are 80% of contract price, repayable over 8½ years from delivery, without moratorium, at a fixed interest rate of 7.5%. BUE Ships require 90% over 11½ years, with an 18 month capital moratorium, at 7.5%.

BUE Ships have been able to arrange a commercial loan from Clydesdale Bank to top the normal Home Credit up to the required terms. Clydesdale are willing to provide this without Government or BS guarantee, but BS would be required to subsidise the interest rate and wish to do so. The NPV cost of this subsidy would be about £720,000, 5.4% of contract price. With normal 15% Intervention Fund, 2% Shipbuilder's Relief and Home Credit with a current NPV of about 8.5%, this would mean a total subsidy value for the contract of 30.9%, £4.14 million. In the context of the increased level of Intervention Fund which we have proposed to the Commission, and the case by case help that is regrettably necessary in the current market situation, this element of the package, I would suggest, should be acceptable.

However a more difficult question arises over the security for the Home Credit Scheme loan of £10.72 million. To meet the conditions recommended by the Ship Mortgage Advisory Committee, BS would be required to provide a guarantee of £5 million for the repayment by BUE Ships of the loan, for a minimum period of four years from delivery. This period might need to be extended if the vessel, which is to a new design, were not performing satisfactorily or if its value, together with any collateral security that BUE was then able to offer, did not provide sufficient security for the loan. The risk of the guarantee being called or extended therefore depends critically upon the performance of the vessel, on which the future of BUE to a considerable extent rests.



I have considerable reservations about permitting BS to provide a guarantee of such a substantial proportion of the contract price for such a period and with such uncertainty about its release. I am also mindful of the total exposure of BS on guarantees. Nevertheless, the pressing need of Smiths Dock for the order and the other factors which I have described above concerning the prospects for the successful privatisation of BUE persuade me on balance to recommend the case to you, with Kenneth Baker's support. You will appreciate that it falls clearly within the agreed guidelines for the provision of yard-supported soft credit for bona fide UK customers.

I should therefore be grateful for your agreement to my consenting to BS providing both the interest subsidy of about 5.4% of contract price in NPV terms and the £5 million guarantee. There is considerable urgency in this case if BUE Ships are to have the vessel available in 1985 to meet the Hamilton charter without incurring either excessive penalties for delay or, indeed, the risk of losing the charter. I should therefore be grateful to have your approval as soon as possible.

I am copying this letter to the members of E(A) and to Alick Buchanan-Smith who supports the case.

*Yours  
Norman*

NORMAN LAMONT

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JU480

Secretary of State for Trade and Industry

8 June 1984

The Rt Hon Peter Rees QC MP  
Treasury Chambers  
Parliament Street  
London SW1

*D Peter*

BRITISH SHIPBUILDERS PAY 1984/5

As you know, British Shipbuilders (BS) last year offered no general pay increase to their employees. National negotiations broke down and the industry went to the brink of a national strike. In the end the unions backed down and accepted a £7 pw payment in return for acceptance and implementation of wider ranging changes in working practices.

2 BS are, I think rightly, pleased with what they achieved last year. They believe that the deal in principle allows them to match the best European working practices. They are now well into the phase of implementing the changes. They have been accepted by all the yards except Vosper Thornycroft, and Vosper Shiprepairers. Yard management are already beginning to see the first indications of a declining trend in unit labour costs. And as BS point out, all this was achieved with only a 0.5% increase in the wage bill last year, as against 13-14% in previous years.

3 What they are aiming at for this year is a period of consolidation. They want principally to push ahead with the changes in working practices to get the full benefit of the deal, and to consolidate effectively, they see in turn the need to minimise the risk of industrial action. The end of June will anyway see the first large set of compulsory redundancies declared (at Cammell Laird) and this in itself could prove a flashpoint. They want both to avoid adding fuel to the fire and to avoid the commitment of senior management resources on the scale which proved necessary last year. They are clear that a repeat of last year's battle would be at the direct expense of the prime Corporate aims of restructuring, getting new orders and privatising warshipbuilding.

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4 There is already on the table the usual demand from the unions for a "substantial" pay increase in 1984/5 and various other benefits. BS will meet them for substantive talks on 18 June. They propose to enter into negotiations with the aim of agreeing a package with 4% overall. It will be carefully structured to enhance differentials, compressed by last year's £7pw; at the extremes some management will be offered 6%, unskilled workers 2%.

5 BS recognise that such an offer is above the 3% guideline, but make the valid point that over the last two years the total increase amounts to only 6.25%, well below the aggregate of the guidelines for these years. They would not of course be seeking any extra funding above the already agreed EFL.

6 I have naturally considered whether BS could not achieve the same result within a lower bracket - say 3 to 3½%. But BS are clear that operating within this limit would not only put the securing of a settlement itself at risk but would also mean the loss of the elements that are of the most enduring benefit - reward to management, the widening of differentials, and the enhancement of shift and other allowances designed to improve working methods. BS judge that they could not reduce further the proposed offer to the unskilled, which is already below 3%.

7 I conclude that BS's proposal makes sense. It is strategically right to consolidate the gains of last year. It is particularly important to get the management right - the right people in the right jobs with the right salaries - and to do everything possible to improve operational performance. And almost the last thing we want is another year of bitter pay negotiations and industrial action. BS took the battle to the unions last year and won. Apart from the deal itself, one of the major gains was the weakening of national union negotiating power. A similar battle this year would risk losing some of that ground, and it would risk holding back the achievement of our prime aim for the industry, including privatisation.

8 I recognise that, taken in isolation against the backdrop of BS's losses, this offer looks generous. It is for this reason that I have set out in some detail the thinking behind it. The BS Board, including the non-executive Members, are quite firm that the proposed offer is in the commercial interest of the Corporation. I therefore do not propose to seek to dissuade them from making it.

9 Copies of this letter go to the Prime Minister, Jim Prior, George Younger and Tom King.

NORMAN TEBBIT

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~~CCNO~~



NDPM AT 46

Treasury Chambers, Parliament Street, SW1P 3AG

Norman Lamont Esq MP  
Minister of State for Industry  
Department of Trade & Industry  
1 Victoria Street  
LONDON  
SW1H 0ET

June 1984

*Dear Minister*

**BRITISH SHIPBUILDERS - BP RIG CONTRACT**

Thank you for your letter of 29 May setting out the considerations which led BS to renegotiate this contract rather than cancel it. This certainly seems to have been the right decision.

I agree that we should look again at the effect of the costs on the non-warship EFL later in the year when other related matters are clearer. It is, of course, important that BS should find offsets wherever possible.

I am copying this letter to the recipients of yours.

*Yours sincerely*

*J. Rees*

J. PETER REES

[Approved by the Chief Secretary]

NAT IND : Shipbuilding : PEB.



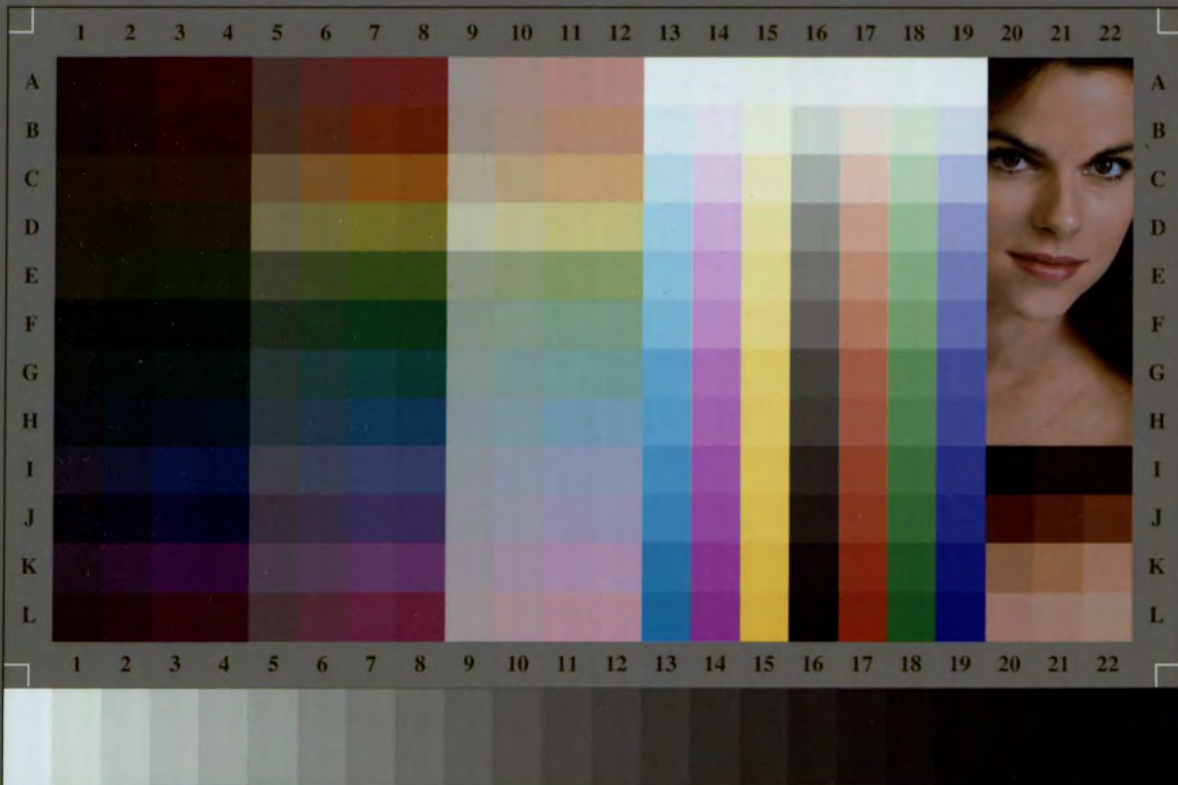
12 JUN 1981  
12 JUN 1981

PART 6 ends:-

Sir W. Salomon to C. Ryder 30.5.84

PART 7 begins:-

CST to M/S DTI June 1984



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