

PREM 19/2785

SECRET

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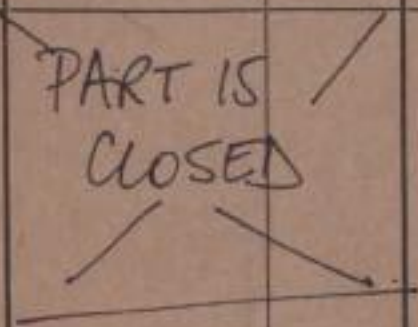
SHIPBUILDING POLICY

SHIPBUILDING PAY

NATIONALISED
INDUSTRIES

Part 1: May 79

Part 15: Oct 88

Referred to	Date	Referred to	Date	Referred to	Date	Referred to	Date
5-10-88		PART 15 CLOSED 					
18-10-88							
24-10-88							
26-10							
31-10-88							
3-11-88							
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PREM 19/2785

PART 15. ends:-

CST to Min S/Wed 17.7.89

PART 2. begins:-

Hawell H. Hughes to Phr 18.12.89

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.

House of Commons. Session 1988-89
Trade and Industry Committee - Third Report
The Privatisation of Harland & Wolff PLC
Ordered to be printed 15 February 1989
Published by HMSO

Signed

J. Gray

Date

22/10/2016

PREM Records Team

ccfu.



Treasury Chambers, Parliament Street, SW1P 3AG

Lord Trefgarne
Minister of State for Defence Procurement
Ministry of Defence
Main Building
London
SW1A 2HB

NBAM

REC 18/7

17th July 1989

Dear David,

PRIVATISATION OF HARLAND AND WOLFF

flat

Thank you for sending me a copy of your letter of 11 July to Tom King.

I confirm that I am content that you should proceed as you suggest, and that our officials should agree the line that should be taken in public presentation of the payment of £22.5 million to Harland and Wolff in settlement of all outstanding claims on the ATS. That line would also form the basis of your Accounting Officer's defence of the transaction before the PAC.

As indicated in Tom King's letter of 10 July, I fully accept that your Defence Budget should be compensated for this payment. I note that it is likely that you will need to have recourse to the Contingencies Fund in advance of obtaining the necessary Parliamentary approval. As you recognise, this will need to be reported to Parliament by means of a Written Answer before the Recess. Our officials are in touch on that and on the modalities for compensation.

I am copying this letter to the Prime Minister and Tom King

Yours Ever,
John

JOHN MAJOR

NAT IND: Mupfuiday Pkwy Pt 15

TR 101 1989



the department for Enterprise

The Rt. Hon. Tony Newton OBE, MP
Chancellor of the Duchy of Lancaster and
Minister of Trade and Industry

Stephen Catling Esq
Private Secretary to the
Lord President
Privy Council Office
Whitehall
LONDON SW1A 2AT

Department of
Trade and Industry

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Our ref
Your ref
Date

215 5147

13 July 1989

Dear Stephen

NORTH EAST SHIPBUILDERS LIMITED (NESL): STATEMENT

I attach a copy of the draft statement which the Chancellor of the Duchy proposes to make later today on North East Shipbuilders.

I should be grateful for any comments on the draft by, if possible, 12.30 pm today.

I am sending a copy of this letter and attachment to Paul Gray (Prime Minister's Office), Alan Ring (DoE), Peter Wanless (Treasury) and Murdo Maclean (Chief Whip's Office).

Yours

John ALTY

JOHN ALTY
PRINCIPAL PRIVATE SECRETARY

RC5ABZ



Mr Speaker, with permission, I wish to make a statement about the disposal of NESL, whose closure was announced last December.

On 7 June, I told the House that four expressions of interest had been received. I said that I proposed to ask BS for advice, which the Government would then weigh alongside a number of other factors before reaching a decision: I explained in particular the need to consider the position under the Sixth Directive, and the relationship between any proposal for shipbuilding [and] the alternative of disposal to the Tyne and Wear Development Corporation [and the continuing justification for measures put in place to assist job creation in Sunderland following the closure of NESL].

I will first comment briefly on the four expressions of interest. Two are from shipbuilding interests. While they vary in the anticipated use of the yards, especially in the short term, both envisage initial employment of about 200, rising to around 1000 at some later date. Of the non-shipbuilding bids one is concerned only with the Pallion Yard; it envisages employing about 250 people initially rising to 600 at a later date, on work connected with desalination projects, floating harbours and offshore oil equipment. The other envisages employment of 400 initially, rising to some 1,650 in three years, to manufacture a waste disposal system which has been demonstrated, but not yet

exploited, in Canada. The advice I have received from BS is balanced. Of what it regards as the better of the two shipbuilding bids, it notes the continued risk to secure long term employment from the market and levels of productivity capable of achievement in the yard against previous experience. Of what it regards as the better of the two non-shipbuilding bids, it says that it could represent the basis for a new and substantial activity but there are a number of important aspects which require further elucidation before clear advice could be given on the prospects of secure employment.

The second factor is the importance attached in Sunderland to the EZ, which was emphasised to me on all sides when I visited the town again at the end of last month. I was told that the Zone has attracted an unusually high level of interest, notably from potential overseas inward investors, and that it would be expected to produce well over 3,000 jobs in the next few years.

Thirdly, we have had to take account of the position under the Sixth Directive on state aid to shipbuilding, under which a variety of measures connected with British Shipbuilders, including the sale of certain assets, the anticipated closure of NESL and some aspects of the remedial package for Sunderland were notified to, and accepted by, the Commission at the turn of last year.

We have always made clear in the House, and to the shipbuilding interests purchasing the yards as they have come forward, that any major change in the arrangements agreed by the Commission would necessarily mean notifying to them a revision, with some uncertainty about the outcome. This uncertainty could only be resolved by an actual renotification, leading to an actual decision by the Commission as a whole. However, the soundings we have taken with the Commission suggest that they would be likely to insist on a procedure, entailing an opportunity for all 11 other Member States to comment; that this process would take some four to six months and that the probable outcome would be for any prospective purchaser of NESL to have to take on at least a significant share of the market borrowing British Shipbuilders requires in respect of past losses that cannot be accommodated within the Sixth Directive. The sums could be significant. No less important, we could not exclude the possibility that the whole of the Sunderland Enterprise Zone, on which we decided last December and which also requires EC agreement, would be called into question.

Mr Speaker, having carefully weighed all these considerations, our view is that the essential choice is clear. On the one hand, the shipbuilding bids, giving at best an uncertain prospect of fewer jobs than before in an industry which has always been subject to cyclical swings. On the other, the vigorous and whole-hearted pursuit of the Enterprise Zone as planned, including the Southwick yard,

coupled with further work on the use of the assets for purposes other than shipbuilding.

We have concluded that the latter course is the best in the long-term interests of Sunderland. Accordingly, I am asking British Shipbuilders to undertake further work on the bids for purposes other than shipbuilding, in consultation with the Tyne and Wear Development Corporation, with a view to making final recommendations in due course. The establishment of the Enterprise Zone, and all other elements in the package of measures to promote enterprise and new jobs in Sunderland, will be pressed ahead with all possible speed and vigour.



10 DOWNING STREET

LONDON SW1A 2AA

From the Private Secretary

11 July 1989

SUBJECT CC MASTER.

NORTH EAST SHIPBUILDERS LIMITED

Mr. Bob Clay M.P. came to see the Prime Minister in the House this afternoon to raise his concerns about the future of NESL.

Mr. Clay said that he understood two shipbuilding bidders, both approved by British Shipbuilders, wished to acquire NESL, with neither pressing for Intervention Fund assistance. But it now appeared that, at the last minute, the European Commission were raising new difficulties about these bids. In the past it had been understood that, as long as no Intervention Fund assistance was sought, there would be no problems over Commission approval of bids for NESL. But the position now seemed to have changed, with the Commission claiming that an old £90 million commercial loan to British Shipbuilders was an obstacle to any new bids being approved. He strongly urged the Government to agree to put forward one of the two bids to the Commission, so that the responsibility for rejecting the proposal would be seen to fall clearly at the door of the Commission and not of the UK Government.

The Prime Minister said that the Chancellor of the Duchy would be making a statement about the future of NESL as soon as possible. But Mr. Clay would have to bear in mind that, if a shipbuilding bid was allowed to proceed, this would be likely to result in a substantial part of the package of assistance for Sunderland being foregone.

Mr. Clay repeated his earlier points, and added that it was his belief in two years time there would be a revival of demand for shipbuilding: it would be a tragedy if meantime one of the best equipped yards in the UK was shut down. This made it all the more important for the Government to ensure that the Commission acted reasonably. It was absurd that, given the earlier objective of moving to non-subsidised shipbuilding in Europe, the Commission did not now welcome proposals from bidders prepared to put in their own money without any request for financial assistance. He added that the ship brokers Clarksons, who were associated with the Greek bid, had asked

him to express their dismay that the Government should be prepared to let the Commission get away with the approach they were adopting.

The Prime Minister said that it was right for the Commission to scrutinise rigorously all proposals for state aids; this approach was to the UK's advantage overall. But she had listened attentively to what Mr. Clay had said and she would pass on the points he had made to the Chancellor of the Duchy who was carefully considering the position.

(PAUL GRAY)

Ms. Rosalind Cole,
Chancellor of the Duchy of Lancaster's Office.

PRIME MINISTER

NORTH EAST SHIPBUILDERS LIMITED
Mr Newton's minute of 7 July

DECISIONS

Mr Newton wants to make an early announcement that the two shipbuilding bids for the facilities at North East Shipbuilders Limited (NESL) are not being pursued and that the remedial measures for Sunderland announced last December are being reinstated. You may wish to agree.

2. On handling, you may wish to ask the Lord President whether the announcement could be made by Written Answer, like the announcement on 7 June, rather than an oral statement.

BACKGROUND

3. E(A) on 6 June agreed that British Shipbuilders should evaluate four bids for NESL's facilities. Since two involved a return to shipbuilding, work on the Enterprise Zone in Sunderland and, so far as practical, the rest of the remedial package was stopped during the evaluation. Parliament was informed. Leon Brittan has now said that the Commission might take a hard line on any resumption of shipbuilding in Sunderland and that a formal examination lasting up to 6 months could be required.

ISSUES

Options

4. Mr Newton's paper describes two options:

i. option A would be to nominate the German shipbuilding bid (Oldendorff and Dohle) and renotify the Commission of last December's shipbuilding package. The Enterprise Zone, excluding the Southwick yard, and some other parts of the remedial package would go ahead;

ii. option B would be not to pursue any shipbuilding bid

but to proceed with the full remedial package announced last December. British Shipbuilders would take steps to dispose of all NESL facilities, in consultation with the Tyne and Wear Development Corporation, in a way which left open the possibility of disposal of one or more sites intact, for instance to Strategic Alloys if their bid became more convincing over the next few months.

5. Mr Newton recommends option B because the balance of advantage for Sunderland lies in continuing with the remedial measures rather than suspending them for at least 6 months in the hope that the German shipbuilding bid could eventually proceed with European Commission approval. He expects the announcement to be difficult because local interests in Sunderland will want both the remedial measures and continued exploration of the shipbuilding bids. You may wish to agree that no shipbuilding bid should be pursued and that the remedial package should be reinstated.

Future of the NESL facilities

6. Although Mr Newton proposes that shipbuilding bids should not be pursued, his description of Option B suggests that one or more of NESL's sites will be left intact. You might want to ask how he will prevent more shipbuilding bids from emerging in the future, after the Government has designated the Enterprise Zone. So far the Government has only been committed to keeping NESL's assets intact until 30 June.

HANDLING

8. You could invite the Chancellor of the Duchy of Lancaster to introduce the item briefly and then ask whether there is general agreement with his proposal.

R.T.J.

R T J WILSON
Cabinet Office
11 July 1989

Alina

dti

H H C.P.U

the department for Enterprise

The Rt. Hon. Tony Newton OBE, MP
Chancellor of the Duchy of Lancaster and
Minister of Trade and Industry

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Private Secretary to
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Date

215 5147

11 July 1989

Dear Paul,

STATEMENT ON NORTH EAST SHIPBUILDERS LIMITED (NESL)

will he?
In his minute of 7 July to the Prime Minister, the Chancellor of the Duchy said that he would circulate a draft statement prior to the E(A) meeting on 12 July. The attached is such a draft and the Chancellor would no doubt wish to consider further amendments in light of the discussion at E(A).

I am copying this to Private Secretaries to E(A) members and to the Private Secretary to Sir Robin Butler.

*Yours
Rosalind Cole*

ROSALIND COLE
PRIVATE SECRETARY

RC6AAW



Recycled Paper

DRAFT STATEMENT

I informed the House on 7 June that I had asked British Shipbuilders to evaluate the four expressions of interest which had emerged in purchasing the assets of NESL at Sunderland. I have now received the advice I sought from the Chairman of British Shipbuilders and the Corporation's financial advisers. It is that, while the two bids which relate to shipbuilding are of higher quality than those received when buyers were sought last year, there remain real doubts about the scale and long-term security of the employment they would provide; and that the two bids for purposes other than shipbuilding do not at present stand up to close examination.

The Government have considered this advice in the context of the wider factors to which I referred on 7 June. We have taken particular account of two factors. The first relates to the EC dimension. I made clear in my statement of 7 December that the Commission would wish to look again at the package if there were significant changes. It is now clear that in relation to a specific proposal of the kind envisaged in the shipbuilding bids, the European Commission would regard it as necessary to carry out a formal investigation in consultation with other Member States of the compability of the proposals with the Sixth Directive on

aid to shipbuilding thus entailing many further months of uncertainty. Although the outcome could not be predicted it seems likely that any new owners would need to take on financial liabilities reflecting previous losses made by BS.

The second is the degree of interest shown by new companies in taking advantage of the opportunities presented by the proposed Enterprise Zone to generate employment to replace that formerly provided by shipbuilding.

In these circumstances, it is plain that to nominate as preferred bidder any of the parties which have expressed interest could only lead to a further lengthy period of uncertainty and risk undermining the drive for a new industrial future for the area. We therefore intend to proceed with the remedial package as announced last December. The Southwick facility will be incorporated, as planned within the EZ. BS will also proceed to dispose of the assets at the Pallion and North Sands facilities, if possible on a basis which allows them to remain in use on site.



Minister of State
for Defence Procurement

D/MIN(DP)/DGT/5/1/9

MINISTRY OF DEFENCE
CONFIDENTIAL WHITEHALL LONDON SW1A 2HB

Telephone 01-218 6621 (Direct Dialling)
01-218 9000 (Switchboard)

11 July 1989

Dear Tom,

PRIVATISATION OF HARLAND & WOLFF

Thank you for your letter of 10 July 1989. I am replying in the absence of George Younger overseas. *attached*

In the light of the circumstances you outline, I am prepared to agree what you propose subject to the following conditions:

- a. The payment of £22.5M to Harland & Wolff plc is conditional on the successful completion of privatisation in the way now proposed.
- b. The payment will formally extinguish all potential MOD liabilities in respect of the contract for the Aviation Training Ship.
- c. The Defence Budget will be reimbursed for the full amount of the £22.5M payment by PES transfer from the NIO, or by other means if they would be preferable in order to make the transaction justifiable to the MOD Accounting Officer concerned.

The Rt Hon Tom King Esq MP

CONFIDENTIAL

CONFIDENTIAL

d. The MOD Accounting Officer is enabled to defend the transaction to the PAC on the overall grounds on which it was made.

I am not sure whether you envisaged keeping aspects of the payment arrangements confidential. I do not believe this will be feasible in practice. If the payment has to be made very soon, it will have to come from the Contingencies Fund (subject to the agreement of the Treasury Accounting Officer), and this must be reported to Parliament before the recess by means of a Written Answer. It will in any event be necessary for the MOD to take a Supplementary Estimate and to expand the ambit of the relevant Vote. It will therefore be necessary for our officials to get together as soon as possible to agree a public line on the assumption that the matter will become public knowledge and to agree the associated arrangements.

I should be grateful to know that you, and John Major to whom I am copying this, are content to go ahead on this basis.

I am copying this letter and yours of 10 July to No 10.

Yours,
David.

Lord Trefgarne

CONFIDENTIAL



NORTHERN IRELAND OFFICE
 WHITEHALL
 LONDON SW1A 2AZ

SECRETARY OF STATE
 FOR
 NORTHERN IRELAND

→ PA

Price Mike

*Cabinet not too long has
 told ya. It does not
 seem to be getting resolved.*

Rt Hon George Younger TD MP
 Secretary of State for Defence
 Ministry of Defence
 Main Building
 Whitehall
 LONDON
 SW1A 2HB

ms

*Rec 6
 12/7*

10 July 1989

Dear Secretary of State,

PRIVATISATION OF HARLAND & WOLFF

I am facing a major difficulty - in terms of both presentation and timing - in persuading the EC to approve the deal privatising Harland & Wolff, and seek your help and co-operation in resolving the outstanding problem.

The background is that my officials negotiated and agreed with DGIV officials a presentation of the proposals which appeared to be acceptable. When it reached Sir Leon Brittan, however, he felt one aspect of it raised great problems for him in the context of the extremely close interest which other Member States are taking in some current DGIV decisions. This does not concern the proposed assistance to the MEBO/Olsen group, where the Commission has proposed a number of difficult but, in my view, manageable changes, but relates to past assistance to H&W which Leon believes represents excess state aid of £22.2m. While we had believed that DGIV officials accepted our arguments in favour of regarding this sum as restructuring rather than operating aid, Leon himself remains concerned about possible implications for other cases. His concern arises out of the EC decisions to confront a number of major state aid cases involving, among others, the Spanish (over shipbuilding) the French (over their car industry and steel) and the Italians

(also on shipbuilding). Leon is not therefore prepared to endorse our notification, and on that the MEBO/Olsen privatisation currently hangs.

He has also, through his officials, discovered the existence of the outstanding claim for £45m made against your Department by H&W in respect of the RFA Argus, the Aviation Training Ship delivered in March 1988. He has suggested that we resolve this ATS claim between us and use the proceeds to H&W to offset what is to him an unacceptable £22.2m subsidy provided by Government to H&W in respect of past losses.

I would therefore ask you to consider making an immediate settlement of the £45m claim. If you were to do so on the basis of half of that claim, that would certainly meet the requirement. I appreciate that to make such a settlement might leave MOD in the undesirable position of implicitly accepting a liability of £22.5m on ATS which MOD still wishes to challenge. I suggest to you however that we need to think of wider considerations than just ATS: if we cannot satisfy Leon and the Commission, then it is my very clear view that the privatisation deal with MEBO/Olsen will collapse. There are no other viable alternatives on the horizon (and even if there were, we would almost certainly face similar EC problems). We would thus face the very real prospect of a somewhat chaotic rundown and closure of H&W. Quite apart from the major political and economic problems that that would pose for me, it would leave MOD with an only partially completed AOR 01. The cost of completing it, as the last ship in a closing H&W, would be very high indeed. Even if it were a practicable proposition to complete the vessel elsewhere (which, given the build stage

which it has reached I frankly doubt) the cost to HMG of completing it away from H&W would be enormous -much more, I suggest, than the proposed £22.5m payment on the ATS claim. I hope very much therefore that you will be able to agree to my proposal.

I understand that the Chief Secretary has accepted that the Defence Budget should be compensated for this payment, and is content for the most appropriate form of compensation to be settled in due course.

I recognise that there may be difficulties in this proposal, but I believe that it represents the only feasible way forward and that the difficulties can be resolved. However, time is not on our side and while we would not need to implement the arrangement until September, there is the most pressing urgency to reach agreement on the way forward by early Tuesday. That deadline is necessary to enable the EC to formally endorse the privatisation agreement before they break for the summer and that, in turn, is crucial if we are to consummate the deal with the MEBO/Olsen group.

I hope that you, or David Trefgarne, will be able to agree to what I have proposed in the course of today. Given his close interest in the H&W disposal, I am copying this to John Major.

Yours sincerely

Simon Sparrow.

TK

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

J J

CONFIDENTIAL

PAUL GRAY

7 July 1989


NESL

Newton was given the chance by E(A) last month to construct a robust case for re-establishing shipbuilding in Sunderland under German or Greek ownership. He has been unable to do this and, as recently as yesterday, firmly intended to renounce private shipbuilding proposals in favour of the original enterprise zone scheme. On the evidence which I have seen, set out in a letter from British shipbuilders attached at Annex A, I believe this is the right course.

I understand that Newton will now also present an alternative 'halfway house' idea without supporting it. This will be set out in a paper later tonight and will propose the sale of one shipyard (Southwick) to the Germans with a reduced enterprise zone elsewhere in the region. The Pallion yard, which is outside the enterprise zone, would close as originally proposed. There does seem an element of dither about such a proposal and, on the basis of the BS letter, it should be discouraged.

Tony
Newton
has now
decided
not to do
= this.
P.C.C.

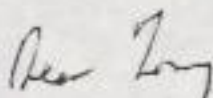
It was right to support Newton last month. Just as the DTI must be discouraged from picking winners, so must the Treasury be discouraged from picking losers! If a commercially robust case for continued shipbuilding in Sunderland had emerged, it would have been wrong to have rejected it purely for dogma. No such case has emerged and we should now go back to square one.


GEORGE GUISE

CONFIDENTIAL

JL37L1
3 July 1989

The Right Hon Anthony H Newton OBE MP
Chancellor of the Duchy of Lancaster
and Minister for Trade
1 Victoria Street
LONDON SW1H 0ET



Privatisation of NESL

In response to your request I and my team have discussed four expressions of interest in the purchase of NESL with the bidders. In this exercise the Corporation have been assisted by their merchant bankers, Lazard Brothers and Company Limited. A copy of Lazard's written advice will follow as soon as possible.

Northern Engineering and Marine Company Ltd (NEMCO)

This is a new company which operates from Darlington. The three Directors are Messrs A Duffield, G M Murray and N F Brownell. NEMCO propose to purchase the Pallion Shipyard for £3.25M. Apart from general engineering sub-contract work, NEMCO envisage three main activities:

1. Agro Forestry. Manufacture of plant for the creation of forestry projects in arid areas by production of fresh water by desalination using a solar energy principle.
2. Flexiports. The manufacture of the Flexiports system of floating harbours for the poorer nations of the world.
3. Offshore oil related with particular reference to subsea templates and redundant platform recovery.

.../2/...

3 July 1989

Although they anticipate employing about 250 people at Pallion within three months and 600 by the end of the first year, NEMCO were unconvincing about their ability to secure projects and have not supplied information on their financial backers. It is pertinent that Mr Duffield was founder and Managing Director of ITM Offshore Limited which went into liquidation losing the Corporation substantial amounts. NEMCO's chosen markets are in Third World projects where there is substantial competition. The technology proposed for the desalination project is not yet proven. The forecast returns shown in their business plan are regarded as unrealistically high.

I could not recommend this bid as a likely source of secure and lasting employment.

Kappa Maritime Limited

Kappa Maritime are Greek Shipbrokers whose registered office is in London. They are being supported by H Clarkson and Company, also shipbrokers. They are also joined by and connected with Transman Shipping Enterprise S/A and Chartwell Maritime, both Greek shipping companies. Satisfactory bank references have been provided. This consortium perceives an upturn in the shipbuilding market when shipowners will be asked to pay high prices for their ships. As a hedge against this and also to make profits, Kappa propose purchasing either the whole of NESL or Southwick and North Sands, excluding Pallion. They are offering £7.5M and £5.7M respectively with a commission of 2% being payable by British Shipbuilders to H Clarkson and Company.

Kappa would commence operations by undertaking two conversions together with an order for the building of two 24,000 dwt multi-purpose TEU container vessels with an option for two further vessels. Both the initial conversions and new buildings would be for the consortium's own fleet. Kappa envisage that these fleets would provide a base load for the future although they would also look for further outside work. Employment is expected to start at 200 rising to 1000 within eighteen months.

Kappa have made clear that their commitment to the project would depend on cost levels achieved on the first two ships and an assessment of further improvements that might be in prospect. The sterling dollar exchange rate would need to be favourable and their judgement about a recovery period in the shipbuilding market confirmed. While they have not seriously investigated likely

3 July 1989

production costs in the yards as organised by themselves, their view of what should be achievable using best practice methods, the market, and sterling lead them to regard this investment as an acceptable risk against the private resources they would employ.

While the Corporation's view is that the shipbuilding market is now embarked on a period of recovery which could last several years, and productivity levels in the yard could be substantially improved with an entirely new start, there must be some doubt that this proposal could be regarded as the basis for secure and lasting employment.

Oldendorff

Egon Oldendorff is the largest private German tramp shipowner. The company has considerable resources, a large fleet and has already built eleven ships at NESL. Their bid is in partnership with Peter Dohle, similarly a conservatively financed private German shipping company with considerable resources.

Like Kappa, Oldendorff and Dohle envisage an upturn in the market and are very concerned that they are going to be at the mercy of shipbuilders in the near future. Unlike Kappa, however, they envisage that their own requirements would occupy NESL for the foreseeable future and that third party work would be a small part of the orderbook initially. They would place an order immediately for a minimum of four ships, hoping to employ 200 people, rising to 1100. They would build hulls at Southwick, outfit at Pallion and, where necessary, fit high superstructures at North Sands. Subject to the approval of the European Commission, they would also envisage building at Pallion in due course. Their offer is £7.5M for the whole of NESL.

While Oldendorff and Dohle maintain that their acquisition of NESL would represent a considerable commitment which they would not give up lightly, and they have investigated prospects with the assistance of a leading shipbuilder, Burmeister and Wein of Denmark, the success of their business would still depend upon the market, the quality of management they were able to attract, and the productivity levels they could achieve. The Corporation regards Oldendorff as a more credible bidder than Kappa but there must still be some doubt about the viability of the venture against the various uncertainties. I believe, however, that the prospect would last longer than the Greek proposal if the market proved less attractive.

.../4/...

Strategic Alloys Limited

Strategic Alloys Limited is a relatively small engineering holding company based at Hemmel Hempstead. Their proposal involves the use of all NESL's facilities to produce a waste disposal system based on technology demonstrated, but not yet exploited, in Canada. The company has plans to build and test a Mark 4 prototype at Redruth in Cornwall in order to demonstrate the process and its compliance with environmental standards by the end of the year.

If the process performs as claimed it will produce gas for its own use with a surplus for re-sale and reduce waste to carbon char which itself is a potentially valuable fuel. Unsuitable materials sorted prior to the treatment would require only 10% of normal land fill. The process, therefore, has many potentially attractive features but market research has so far been limited.

Strategic Alloys point out that the facilities at NESL are ideal for early production of their system on the significant scale they believe would be necessary to secure a place in a market which is likely to become competitive once their process has been demonstrated. Pallion would be used to build the central furnaces, Southwick to manufacture ancillary equipment, and North Sands to build barge mounted sets. They have offered a negotiable bid of around £7.5M to £8M for the whole of NESL, but it is known that they hope to attract regional selective assistance from the DTI towards this project.

If Strategic Alloys' proposals were successful, employment would rise from 400 initially to some 1650 in three years. However, as they stand and despite general promise, their proposals do not adequately explain how production, management, marketing or financial support would be provided. Urgent discussions are in progress with Bovis on several of these aspects.

Conclusion

Of the two shipbuilding interests, Oldendorff's is the more attractive although there would still be risks to secure long term employment from the market and levels of productivity achievable in the yard. The Sixth Directive could be relevant to either shipbuilding proposition and the Corporation would be concerned if renotification of proposals for NESL to put other disposals at risk.

The Right Hon Anthony H Newton OBE MP
-5-

3 July 1989

On the two non-shipbuilding interests, NEMCO's proposals are unconvincing. Those from Strategic Alloys could represent the basis for a new and substantial manufacturing activity but there are a number of important aspects which require further elucidation before I could give clear advice on the prospects for secure employment.

John

TO:

PRIME MINISTER

FROM:

TONY NEWTON

7 July 1989

NORTH EAST SHIPBUILDERS LIMITED (NESL)

At E(A) on 6 June colleagues agreed that I should request advice by 30 June from British Shipbuilders (BS) on the four parties interested in bidding for the assets at NESL, and that I should discuss with Leon Brittan the Commission's attitude to acceptance of any of the bids under consideration. In the meantime the remedial package for Sunderland agreed last autumn, including the proposed Enterprise Zone (EZ), was put in abeyance, with the prospect that all or part of it might be withdrawn should shipbuilding restart. I announced the terms on which the bids would be considered to the House on 7 June. A copy of my statement is at Annex A.

2. The key elements informing my consideration of the bids have been the advice I have received from BS; my discussions with Leon Brittan; and my meetings with representatives from the relevant organisations in Sunderland.

RC5AAF



Advice from BS

3. I attach (Annex B) a copy of the advice to me from the Chairman of British Shipbuilders. This comments in turn on each of the four bidders. Of the two shipbuilding bids - both considerably better than any we had last year - it concludes that the Oldendorff and Dohle bid is more credible. Any doubts about the proposal are no more than doubts that would be expressed about any large engineering venture with a typically cyclical market. Of the two non-shipbuilding bids, that from Northern Engineering and Marine Company Ltd does not provide convincing evidence of adequate financial backing or ability to secure orders. That from Strategic Alloys is potentially more interesting but has not yet reached a stage where a clear assessment could be made of the prospects of its generating secure employment.

Compatibility with the Sixth Directive

4. I discussed this with Leon Brittan in Brussels on 27 June. While of course a full and definitive view could be obtained only by putting a specific proposal to the Commission as a whole, Leon Brittan was clear on the view he would press. This was not only that he would want (as we would have expected) to look at the proposal in the context of the shipbuilding package notified and agreed at the end of last year, but that the Commission would want to open a formal procedure to permit an examination lasting up to six months.

5. He made clear that the fact that Intervention Fund was not available would not of itself allow the Commission to take a relaxed view, and that they could be expected to require some arrangement to expose the financial liability

reflecting the large losses previously made by the Corporation, not least at NESL itself. He also indicated that he might wish to press for the Commission to reconsider the Enterprise Zone, which we had earlier been given to understand was regarded (by the Commission, if not by us) as a wholly separate matter.

6. It appeared that his reaction, which showed considerably less flexibility than indications my officials had received earlier in the year, had been influenced by a number of other current state aid cases with which he is dealing, both in the shipbuilding sector itself, where the Commission have opened procedures against the Spanish and Italians, and elsewhere, where they are pursuing the French and Italian Governments for failing to stick to agreements on Renault and Pinsider respectively.

Opinion in Sunderland

7. I visited Sunderland on 28 June, and met representatives of the Northern Development Corporation (NDC), Sunderland Borough Council (SBC), The Wearside Opportunity (TWO) and the Tyne and Wear Development Corporation (TWDC). Predictably, all would prefer both shipbuilding and the remedial package (including, in the case of SBC, an Enterprise Zone to which an area would be added to compensate for taking out the Southwick yard). The NDC, TWO and the TWDC noted the strength of the response to their marketing of the EZ, and their wish to be able to press ahead without further delay. The signs from the EZ are indeed encouraging: the latest estimates are that in excess of 3,000 jobs are likely to be created over the next five years, with substantial interest from inward investors.

f 100 m -
Bid Ship.

Options

8. Against this background, I could not recommend that we should keep the whole remedial package in abeyance while we seek to reach an accommodation with the Commission over a shipbuilding bid. Although the bidders have indicated that the delay involved in a procedure would not itself disrupt their programmes for a resumption of shipbuilding, there could be no guarantee of an acceptable outcome and meanwhile the uncertainty over the fate of the EZ would be unacceptable to Sunderland.

9. Realistically therefore there are only two options:

Option A

to nominate a preferred shipbuilding bidder and proceed to renotify to the Commission the package which was the subject of their decision last December, whilst going ahead with the Enterprise Zone, excluding Southwick, and such other parts of the remedial package as we thought appropriate. The main advantages of this option would be

- it would keep open the possibility of a viable shipbuilding bid which would create upwards of 1,000 jobs - more than the EZ is expected to create at Southwick alone.
- it would avoid some £12½m of redevelopment costs and EZ benefits at Southwick, whilst bringing in £7½m from the private sector. There would however be an additional cost to BS of around

£1m in care and maintenance of the yard during a procedure.

- it would defuse criticism that the Government was not prepared to press the Commission to find a solution to the subsidy problems, which arise as a result of past rather than future assistance.

The main disadvantage would be that we would risk the Commission reopening the disposals of other BS yards.

We would need to ensure that we did not put the EZ (apart from Southwick) at risk, although as that was the subject of a separate Commission decision, I suspect that we could keep it untouched. We would also of course prolong uncertainty over whether shipbuilding was to revive or not, with the possibility of negative outcome at the end of the process.

Option B

To state that we do not intend to proceed further with any shipbuilding bid, and that the full remedial package will be pressed ahead. In this case I would propose that BS should take steps to dispose of all the NESL facilities in consultation with the TWDC in a way which left open the possibility of disposal of one or more sites intact, for instance to Strategic Alloys if their bid became more convincing over the next few months.



The advantage of this option is that it provides greater certainty for Sunderland and focusses the town's energies on the drive for a new industrial future. The disadvantage - not to be under-estimated in presentational terms - is the criticism which will be directed at both the Government and the Commission for turning down what will be widely regarded as a viable shipbuilding bid. This will be aggravated by the fact that, to avoid future difficulties with the Commission, we would have to make arrangements to ensure that no shipbuilding would take place on the site for five years.

Conclusion

10. Had shipbuilding bids of this quality come forward last year, I have little doubt that it would have been right to nominate one of them as preferred bidder and proceed to negotiation. However, the priority now must be to sustain the drive for new, non-shipbuilding, jobs in Sunderland. In practice, this could be secured by going ahead with the EZ excluding Southwick, if colleagues were willing to agree. But on balance, in spite of the severe presentational difficulties we shall face, I believe the better course is to avoid further uncertainty over shipbuilding and to press forward with the whole remedial package.

Fulmer
Perk.

Handling

11. The difficulties a return to shipbuilding would pose for the Commission are by now publicly known and a decision to proceed with the original remedial package would not be unexpected. Nevertheless, there would be considerable disappointment and frustration amongst those who wanted to

see shipbuilding restart, which would be directed both at the Government and the European Commission itself. I have received strong representations from the local MP, Mr Bob Clay, supported by Bryan Gould who has now also taken up the issue with Leon Brittan. Given the strength of Parliamentary interest, I see no alternative to an oral announcement of our decision. I shall circulate a draft prior to the E(A) meeting, I hope it would be possible to make a statement very soon thereafter.

Recommendation

12. I am copying this minute to colleagues on E(A) and to Sir Robin Butler.

TN

Mr. Brooke: Where appropriate a collection charge of 2½ per cent. of the amount of the deduction is made.

Customs Officers

Mr. Denzil Davies: To ask the Chancellor of the Exchequer how many Customs officers were in post at the ports of (a) Fishguard, (b) Pembroke Dock and (c) Holyhead as at (i) 5 April 1979 (ii) 5 April 1984 and (iii) 5 April 1989.

Mr. Lawson [holding answer 6 June 1989]: The numbers of Customs officers in post at the ports of Fishguard, Pembroke Dock and Holyhead at 5 April in the years 1979, 1984 and 1989 were as follows:

	1979	1984	1989
Fishguard	21	22	21
Pembroke	17	18	20
Holyhead	45	39	67

¹excludes four mobile staff not solely engaged in port duties.

²excludes 14 mobile staff.

Mr. Denzil Davies: To ask the Chancellor of the Exchequer how many Customs officers were in post in Britain as of (a) 5 April 1979 and (b) 5 April 1989.

Mr. Lawson [holding answer 6 June 1989]: On 5 April 1979 there were 7,600 Customs officers in post at ports, airports and inland premises. The figure for 5 April 1989 was 8,000.

Value Added Tax Registrations

Sir Anthony Meyer: To ask the Chancellor of the Exchequer what were the numbers of new value-added tax registrations for businesses with registered addresses in Wales for the calendar years 1987, 1988 and for 1989 to date.

Mr. Lilley [holding answer 6 June 1989]: The local VAT offices that cover Wales also cover parts of England along the Welsh border. These offices are at Chester, Cardiff, Swansea, Carmarthen, Shrewsbury and Colwyn Bay.

The numbers of VAT registrations processed by these officers for the years in question were:

Year	New registrations
1987	11,577
1988	14,748
1989—to 31 March	4,061

TRADE AND INDUSTRY

Small Businesses

Mr. David Nicholson: To ask the Chancellor of the Duchy of Lancaster what estimates he has of the number of small businesses with a turnover of less than £1 million which went into liquidation in (a) 1986, (b) 1987 and (c) 1988; and if he will make a statement.

Grade	1 April 1984		1 April 1985		1 April 1986		1 April 1987		1 April 1988		1 April 1989	
	Allocation	Staff in Post	Allocation	Staff in Post	Allocation	Staff in Post	Allocation	Staff in Post	Allocation	Staff in Post	Allocation	Staff in Post
E/DIR/L	1	1	1	1	1	1	1	1	1	1	1	1
INS/GD/A	1	1	1	1	1	1	1	1	2	2	3	3
INS/GD/B	5	5	6	5	7	6	7	8	8	7	12	12

Mr. Maude: I regret that the information requested is not available.

North East Shipbuilders Ltd

Mr. Trotter: To ask the Chancellor of the Duchy of Lancaster what arrangements he envisages for the disposal of the assets at NESL.

Mr. Newton: I made it clear earlier this year, following the announcement that British Shipbuilders was to close NESL, that the remaining work on ferries originally ordered by Danish interests would take some months to complete, and that no action would be taken to break up the assets in the yard before the end of June.

In the intervening period, there have been several expressions of interest in some or all of the yards for a number of purposes including shiprepair, shipbuilding and general engineering.

I have therefore asked British Shipbuilders and its financial advisers carefully to evaluate all such proposals with a view to advising me by the end of this month whether one or more of them provides a basis for detailed negotiation for the disposal of some or all of the assets. As with the evaluation of bids for NESL prior to the announcement of closure particular weight will be given to the security of resulting employment. In judging viability it will be necessary to allow for the fact that subsidy from the intervention fund would not be available.

In making its judgment on the advice offered by British Shipbuilders on any possible disposal, the Government will need also to take appropriate account of its acceptability under the EC sixth directive on shipbuilding of the balance of advantage by comparison with the alternative of acquisition by the Tyne and Wear development corporation for clearance and development; of the extent to which any form of Government financial assistance was envisaged.

Should such a disposal take place, the Government would also have to decide whether measures to assist the creation of employment to replace that in the yards continued to be necessary. Pending a decision, elements of the proposed remedial package not yet implemented, including designation of an enterprise zone, will be held in abeyance.

Companies Investigation Branch

Mr. Cousins: To ask the Chancellor of the Duchy of Lancaster what is the establishment and staff in post in each grade of the companies investigation branch of the Department of Trade and Industry in each year since 1984.

Mr. Forth: The following table shows the posts allocated by grade to the companies investigation branch on 1 April in each of the years in question. Staff in post tends to change in the course of a year. The table, therefore also lists the staff in post on 1 April.

JL37L1
3 July 1989

The Right Hon Anthony H Newton OBE MP
Chancellor of the Duchy of Lancaster
and Minister for Trade
1 Victoria Street
LONDON SW1H 0ET

Dear Tony

Privatisation of NESL

In response to your request I and my team have discussed four expressions of interest in the purchase of NESL with the bidders. In this exercise the Corporation have been assisted by their merchant bankers, Lazard Brothers and Company Limited. A copy of Lazard's written advice will follow as soon as possible.

Northern Engineering and Marine Company Ltd (NEMCO)

This is a new company which operates from Darlington. The three Directors are Messrs A Duffield, G M Murray and N F Brownell. NEMCO propose to purchase the Pallion Shipyard for £3.25M. Apart from general engineering sub-contract work, NEMCO envisage three main activities:

1. Agro Forestry. Manufacture of plant for the creation of forestry projects in arid areas by production of fresh water by desalination using a solar energy principle.
2. Flexiports. The manufacture of the Flexiports system of floating harbours for the poorer nations of the world.
3. Offshore oil related with particular reference to subsea templates and redundant platform recovery.

.../2/...

3 July 1989

Although they anticipate employing about 250 people at Pallion within three months and 600 by the end of the first year, NEMCO were unconvincing about their ability to secure projects and have not supplied information on their financial backers. It is pertinent that Mr Duffield was founder and Managing Director of ITM Offshore Limited which went into liquidation losing the Corporation substantial amounts. NEMCO's chosen markets are in Third World projects where there is substantial competition. The technology proposed for the desalination project is not yet proven. The forecast returns shown in their business plan are regarded as unrealistically high.

I could not recommend this bid as a likely source of secure and lasting employment.

Kappa Maritime Limited

Kappa Maritime are Greek Shipbrokers whose registered office is in London. They are being supported by H Clarkson and Company, also shipbrokers. They are also joined by and connected with Transman Shipping Enterprise S/A and Chartwell Maritime, both Greek shipping companies. Satisfactory bank references have been provided. This consortium perceives an upturn in the shipbuilding market when shipowners will be asked to pay high prices for their ships. As a hedge against this and also to make profits, Kappa propose purchasing either the whole of NESL or Southwick and North Sands, excluding Pallion. They are offering £7.5M and £5.7M respectively with a commission of 2% being payable by British Shipbuilders to H Clarkson and Company.

Kappa would commence operations by undertaking two conversions together with an order for the building of two 24,000 dwt multi-purpose TEU container vessels with an option for two further vessels. Both the initial conversions and new buildings would be for the consortium's own fleet. Kappa envisage that these fleets would provide a base load for the future although they would also look for further outside work. Employment is expected to start at 200 rising to 1000 within eighteen months.

Kappa have made clear that their commitment to the project would depend on cost levels achieved on the first two ships and an assessment of further improvements that might be in prospect. The sterling dollar exchange rate would need to be favourable and their judgement about a recovery period in the shipbuilding market confirmed. While they have not seriously investigated likely

.../3/...

3 July 1989

production costs in the yards as organised by themselves, their view of what should be achievable using best practice methods, the market, and sterling lead them to regard this investment as an acceptable risk against the private resources they would employ.

While the Corporation's view is that the shipbuilding market is now embarked on a period of recovery which could last several years, and productivity levels in the yard could be substantially improved with an entirely new start, there must be some doubt that this proposal could be regarded as the basis for secure and lasting employment.

Oldendorff

Egon Oldendorff is the largest private German tramp shipowner. The company has considerable resources, a large fleet and has already built eleven ships at NESL. Their bid is in partnership with Peter Dohle, similarly a conservatively financed private German shipping company with considerable resources.

Like Kappa, Oldendorff and Dohle envisage an upturn in the market and are very concerned that they are going to be at the mercy of shipbuilders in the near future. Unlike Kappa, however, they envisage that their own requirements would occupy NESL for the foreseeable future and that third party work would be a small part of the orderbook initially. They would place an order immediately for a minimum of four ships, hoping to employ 200 people, rising to 1100. They would build hulls at Southwick, outfit at Pallion and, where necessary, fit high superstructures at North Sands. Subject to the approval of the European Commission, they would also envisage building at Pallion in due course. Their offer is £7.5M for the whole of NESL.

While Oldendorff and Dohle maintain that their acquisition of NESL would represent a considerable commitment which they would not give up lightly, and they have investigated prospects with the assistance of a leading shipbuilder, Burmeister and Wein of Denmark, the success of their business would still depend upon the market, the quality of management they were able to attract, and the productivity levels they could achieve. The Corporation regards Oldendorff as a more credible bidder than Kappa but there must still be some doubt about the viability of the venture against the various uncertainties. I believe, however, that the prospect would last longer than the Greek proposal if the market proved less attractive.

.../4/...

3 July 1989

Strategic Alloys Limited

Strategic Alloys Limited is a relatively small engineering holding company based at Hemmel Hempstead. Their proposal involves the use of all NESL's facilities to produce a waste disposal system based on technology demonstrated, but not yet exploited, in Canada. The company has plans to build and test a Mark 4 prototype at Redruth in Cornwall in order to demonstrate the process and its compliance with environmental standards by the end of the year.

If the process performs as claimed it will produce gas for its own use with a surplus for re-sale and reduce waste to carbon char which itself is a potentially valuable fuel. Unsuitable materials sorted prior to the treatment would require only 10% of normal land fill. The process, therefore, has many potentially attractive features but market research has so far been limited.

Strategic Alloys point out that the facilities at NESL are ideal for early production of their system on the significant scale they believe would be necessary to secure a place in a market which is likely to become competitive once their process has been demonstrated. Pallion would be used to build the central furnaces, Southwick to manufacture ancillary equipment, and North Sands to build barge mounted sets. They have offered a negotiable bid of around £7.5M to £8M for the whole of NESL, but it is known that they hope to attract regional selective assistance from the DTI towards this project.

If Strategic Alloys' proposals were successful, employment would rise from 400 initially to some 1650 in three years. However, as they stand and despite general promise, their proposals do not adequately explain how production, management, marketing or financial support would be provided. Urgent discussions are in progress with Bovis on several of these aspects.

Conclusion

Of the two shipbuilding interests, Oldendorff's is the more attractive although there would still be risks to secure long term employment from the market and levels of productivity achievable in the yard. The Sixth Directive could be relevant to either shipbuilding proposition and the Corporation would be concerned if renotification of proposals for NESL to put other disposals at risk.

The Right Hon Anthony H Newton OBE MP

-5-

3 July 1989

On the two non-shipbuilding interests, NEMCO's proposals are unconvincing. Those from Strategic Alloys could represent the basis for a new and substantial manufacturing activity but there are a number of important aspects which require further elucidation before I could give clear advice on the prospects for secure employment.

John
Newton



me from
21

10 DOWNING STREET
LONDON SW1A 2AA

From the Private Secretary

7 June 1989

SHIPBUILDING STATEMENT

You kindly faxed to me yesterday evening the latest draft of the Chancellor of the Duchy's proposed statement this afternoon following discussions with the Chief Secretary. The Prime Minister has seen this and is content with it.

I am copying this letter to Carys Evans (Chief Secretary's Office).

Paul Gray

John Alty, Esq.,
Chancellor of the Duchy of Lancaster's Office.

Text agreed with Chief Secretary

I made it clear earlier this year, following the announcement that British Shipbuilders were to close NESL, that the remaining work on ferries originally ordered by Danish interests would take some months to complete, and that no action would be taken to break up the assets in the yard before the end of June.

In the intervening period, there have been several expressions of interest in some or all of the yards for a number of purposes including shiprepair, shipbuilding and general engineering.

I have therefore asked British Shipbuilders and their financial advisers carefully to evaluate all such proposals with a view to advising me by the end of this month whether one or more of them provides a basis for detailed negotiation for the disposal of some or all of the assets. As with the evaluation of bids for NESL prior to the announcement of closure particular weight will be given to the security of resulting employment. In judging viability it will be necessary to allow for the fact that subsidy from the Intervention Fund would not be available.

In making its judgement on the advice offered by British Shipbuilders on any possible disposal, the Government will need also to take appropriate account of its acceptability under the EC Sixth Directive on shipbuilding; of the balance of advantage by comparison with the alternative of acquisition by the Tyne and Wear Development Corporation for clearance and development;

of the extent to which any form of Government financial assistance was envisaged [~~and of any reduction required in~~ measures intended to assist the creation of employment to replace that in the yards. Pending a decision, further action on the proposed Enterprise zone will be held in abeyance.]

insert from next sheet.

Should such a disposal take place, the Government would also have to decide whether measures to assist the creation of employment to replace that in the yards continued to be necessary. Pending a decision, elements of the proposed remedial package not yet implemented, including designation of an Enterprise Zone, will be held in abeyance.

mt

Text agreed with Chief Secretary

I made it clear earlier this year, following the announcement that British Shipbuilders were to close NESL, that the remaining work on ferries originally ordered by Danish interests would take some months to complete, and that no action would be taken to break up the assets in the yard before the end of June.

In the intervening period, a number of proposals have been put forward of interest in view of the fact that the yard is still active, including shiprepair, shipbuilding and industrial equipment.

I have therefore, asked British Shipbuilders and their financial advisers carefully to evaluate all such proposals, and to advise me by the end of this month whether any of them provides a basis for restricted liquidation for the disposal of some or all of the assets. It is the Government's policy to close NESL prior to the announcement of the next general election, and to be given to the Secretary of State, or to the Secretary of State, if the viability it will be necessary to provide a subsidy from the resources of the State.

In making its judgement, the Secretary of State will take account of the fact that British Shipbuilders are a public body, and that the Government is also to take account of the fact that the yard is still active, and the EC Sixth Directive on liquidation, which requires that the assets be sold by comparison with the liquidation of a private company, and Wear Development Corporation, and other similar bodies.

of the extent to which any form of Government financial assistance was envisaged [and of any reduction required in measures intended to assist the creation of employment to replace that in the yards.] Pending a decision, further action on the proposed Enterprise zone will be held in abeyance.

insert from next sheet

Should such a disposal take place the Government would also have to decide whether measures to assist the creation of employment to replace that in the yards continued to be necessary. Pending a decision, elements of the proposed remedial package not yet implemented, including designation of an Enterprise Zone, will be held in abeyance.

mt

PRIME MINISTER

SHIPBUILDING STATEMENT

I attach the latest version of Tony Newton's statement for tomorrow, which reflects further exchanges between Tony Newton and John Major in the light of this morning's E(A) discussion.

Content?

Yes *mk*

fcc.

PAUL GRAY

6 June 1989

PRIME MINISTER

MEETING OF E(A): 6 JUNE

You saw over the weekend the main papers (Flags A-C summarised in my earlier minute below) for tomorrow's discussion on North East Shipbuilders Limited (NESL).

I now also enclose two supplementary notes:

- At Flag D. The promised draft Parliamentary Statement proposed by Tony Newton
- At Flag E. A note from Tom King, who cannot attend tomorrow's meeting, supporting Tony Newton's proposed course of action

You may also like to note that there is no need for any discussion on the position at Fergusons. Although some of the earlier exchanges between John Major and Tony Newton are attached to Tony Newton's paper at Flag A, that was a mistake - this particular issue has been sorted out bilaterally between them, and it is only NESL that has to be resolved.

Page

PG

5 June, 1989.

CONFIDENTIAL

PRIME MINISTER

MEETING OF E(A): TUESDAY, 6 JUNE

You saw last weekend the recent exchanges between Tony Newton and John Major on North East Shipbuilders Limited (NESL).

You commented then that you thought John Major had the stronger arguments; and that if one aspect of the earlier deal was re-opened, all aspects would need to be looked at again with possibly disastrous consequences for Sunderland. But you said that, if Tony Newton wanted a meeting of E(A), you would have one.

We discussed this with Tony Newton's Office earlier in the week, and he has come back to say he would like a meeting. This has therefore been arranged for Tuesday.

You are already familiar with the main issues, but you may like to glance over the weekend at the latest papers. These are:

- Flag A Formal E(A) paper by Tony Newton summarising the arguments and attaching at an annex the earlier exchanges of letters
- Flag B Cabinet Office brief
- Flag C Note by George Guise which amplifies the information in Tony Newton's paper about the German and Greek consortia who are interested in purchasing NESL.

Recg.

PG

2 June, 1989.

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the department for Enterprise

DD

ESPO
CCBP

The Rt. Hon. Tony Newton OBE, MP
Chancellor of the Duchy of Lancaster and
Minister of Trade and Industry

Paul Gray Esq
Private Secretary to the
Prime Minister
10 Downing Street
LONDON
SW1A 2AA

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Direct line 215 5147

Our ref

Your ref

Date

5 June 1989

Dear Paul

E(A): 6 JUNE: NORTH EAST SHIPBUILDERS LIMITED

I attach a copy of the draft suggested Parliamentary Answer to a Question on North East Shipbuilders which the Chancellor of the Duchy promised to circulate in advance of tomorrow's meeting.

I am copying this to the Private Secretaries of other members of E(A) and the Private Secretary to Sir Robin Butler.

Yours
John Alty

JOHN ALTY
PRINCIPAL PRIVATE SECRETARY

SB9ABG



I made it clear earlier this year, following the announcement that British Shipbuilders were to close NESL, that the remaining work on ferries originally ordered by Danish interests would take some months to complete, and that no action would be taken to break up the assets in the yard before the end of June.

In the intervening period, there have been several expressions of interest in some or all of the yards for a number of purposes including shiprepair, shipbuilding and general engineering.

I have therefore asked British Shipbuilders and their financial advisers carefully to evaluate all such proposals with a view to advising me by the end of this month whether one or more of them provides a basis for detailed negotiation for the disposal of some or all of the assets. As with the evaluation of bids for NESL prior to the announcement of closure, particular weight will be given to the security of resulting employment. In judging viability it will be necessary to allow for the fact that subsidy from the Intervention Fund would not be available.

In making its judgement on the advice offered by British Shipbuilders, the Government will need also to take appropriate account of the acceptability of any possible disposal under the EC Sixth Directive on shipbuilding; of the balance of advantage between any possible disposal and the alternative of acquisition by the Tyne and Wear Development Corporation for clearance and

development; of the extent to which any possible disposal was likely to entail Government financial assistance other than through the Intervention Fund, for example through Regional Selective Assistance or the Home Shipbuilding Credit Scheme; and of the need consequent upon any possible disposal to review relevant elements in the package of measures to create employment to replace that previously provided in the yards.



E
CCP
etc.

Prime Minister

BRITISH SHIPBUILDERS: NESL

I have noted the recent correspondence between Tony Newton and John Major about the renewed interest in NESL and the possibility that the closure decision might be reconsidered. I am sorry that as a result of longstanding engagements in Northern Ireland I am unable to attend E(A) tomorrow.

I understand very well the difficult political and presentational problems that are now raised and John's understandable concern that, whatever pledges are given in advance by the purchaser, there may nonetheless be potential liabilities in the future if and when the market turns down again.

Nonetheless, I do not believe it is politically realistic for Tony simply to refuse to entertain any bids for the yards without even considering them. I believe that he should ask the interested parties to produce full business plans, and then undertake a really thorough examination of their ability to survive in a very tough market without subsidy.

I am copying this to John Major and Tony Newton and also to E(A) colleagues and Sir Robin Butlef.

TK

5 June 1989

CONFIDENTIAL

SP/20103

(Approved by the Secretary of State & signed in his absence)

NAS md: Shipbilly

P 15



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0512

CONFIDENTIAL

PAUL GRAY

2 June 1989

POTENTIAL PURCHASERS OF NESL

I have obtained the following information about the German and Greek consortia who are interested in purchasing NESL. Some of this information is repeated in annexures to the E(A) paper.

Germans: A joint venture between Egon Oldendorff which own a mixed fleet of cargo vessels and is a long-standing customer of NESL, and Peter Dohle which is the biggest container ship operation in Germany. The joint venture operates about 150 ships, averaging some 30,000 DWT which is a size compatible with NESL facilities. The joint venture has wholly owned total assets of 4 billion DM and is conservatively geared at 28%. It is making 'a lot of money' at the moment, but nobody can tell me exactly how much or what the accounts look like. I am, however, assured that both joint venturers are old, respected businesses which stand by their commitments.

Greeks: This is a joint venture between Kollakis and Manios operating in the UK through Charterwell Maritime and Transman Shipping respectively. The joint venture has 80 ships and bankers references have indicated that it is financially secure for up to \$50 million of borrowing. It currently has 'lots of cash' but again no-one can tell me how much. Neither of the Greeks are old customers of NESL and have tended to buy second-hand vessels.

Comment

Of the two, the Germans sound the more established and reliable and the least likely to embarrass us by demands


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for lots more money after the Yard is bought. However, the Government cannot be secure against that possibility with either purchaser, particularly if the current optimism in the market turns sour.

British Shipbuilders was at the very top of the world cost curve, largely due to inefficient management and costing practices. There is some possibility that a determined customer-owner could operate at a lower cost structure and indeed Sumitomo indicated last year that BS could take at least a third off their costs if they modernised their practises.

It is, therefore, back to the original argument. On purely commercial grounds, these are not purchasers to be dismissed as hollow, like Ravi Tikoo. Their seriousness and creditworthiness have stood up to the DTI's superficial analysis. Before any real negotiation was entered, accounts etc would have to be properly examined. This is not, however, the key issue. That remains the political question of whether we can stomach the accusations of back-tracking articulated by the Chief Secretary against Newton's view that not to take the purchase proposals seriously could do us even more harm.



GEORGE GUISE

CONFIDENTIAL

PRIME MINISTER

P 03459

NORTH EAST SHIPBUILDERS LTD

Paper by the Chancellor of the Duchy of Lancaster:
E(A) (89)18

DECISIONS

Mr Newton wants to announce immediately that he is asking British Shipbuilders to assess all the bids which they have received for buying shipyard assets at Sunderland including in particular two bids from German and Greek interests. Mr Major wants to reject the bids now, and to make it clear that the shipyards will still close as Mr Newton announced last December

2. You will wish to decide what should be said about the approaches which have been received for NESL. The basic judgement is whether to:

i. reject the approaches now, so as to avoid raising false expectations or suggesting that the Government's stance has weakened; or

ii. say that the bids will be assessed, so as to avoid rejecting bids which have not even been considered, and put off a final decision until around the end of this month.

BACKGROUND

3. On 7 December 1988 Mr Newton told the House that:

"I see no further realistic prospect of maintaining NESL in its present form, and its shipbuilding yards will therefore progressively close as the current workload runs out.... Both my predecessors and I have made it clear that, should it not prove possible for shipbuilding

to continue on Wearside, we would bring forward a range of measures to assist those affected and to promote alternative employment in the town....The House will share my regret that, despite every effort, it has not proved possible to find a way forward for NESL. But it must now be right to concentrate on securing a new industrial future for the town."

The remedial package which he announced, at a total cost of £45m, had three elements: an Enterprise Zone for Sunderland; new advance factories; and financial help to encourage new employment opportunities.

ISSUES

Future of shipbuilding market

4. Mr Newton has argued that the latest research shows that supply and demand would be broadly in balance from the mid-1990s, and that demand for the type of ship built at NESL has already increased substantially over the past year. But on 7 December Mr Newton said: "I am not prepared to bank on hopes of an upturn in world shipbuilding which are constantly being revised downwards and which have been further revised downwards in the past few months by the Association of West European Shipbuilders, which suggests that any real upturn will come at best in the latter half of the 1990s, not in the first half as it predicted before". You may wish to ask whether the Government can change its mind so substantially about long term prospects within a few months. It can be argued that it is for the private sector bidders to make up their own minds about market prospects. But the Government has to bear it in mind that if the bidders get their judgement wrong they will come to the Government for help.

Intervention Fund (IF) money.

5. Mr Newton says that he would make it clear to any purchaser that Intervention Fund (IF) support would not be available. He adds that pressure for IF support elsewhere, for example at Swan Hunter, has been successfully resisted. The Chief Secretary thinks that in practice it would be hard to maintain this line, particularly as other merchant yards in the UK have it including those recently privatised. A major judgement for the Committee is whether it will be practical in the long term to resist the pressure for IF money if the shipyards are sold and then run into difficulty.

6. The Chief Secretary points out that under the Home Shipbuilding Credit Guarantee Scheme soft loans would be available to shipowners ordering from the NESL yards. This would be extra public expenditure. You might ask how much money might be involved.

The remedial package.

7. Mr Newton said on 7 December that the remedial package was proposed "should it not prove possible for shipbuilding to continue on Wearside". You might question whether it would be right to proceed with the full package if shipbuilding could after all continue. Mr Newton accepts that there is a problem here, and proposes to "explore the scope" for reducing the size of the package by for example taking the shipyards out of the Enterprise Zone. You may wish to ask whether a modification of the package is now technically and politically practical. There is also the point that NESL would be re-employing many of those recently made redundant by British Shipbuilders with payments around £11,000 each.

European dimension.

8. Mr Newton reports the UKREP advice that the Commission would be "unlikely" to let the reopening of NESL affect their handling of other state aid cases such as Harlands and Shorts. But he

proposes to talk informally to Sir Leon Brittan to make sure. You may wish to get the views of the Foreign Office Minister on this question.

Government Statement.

9. The immediate decision for the Committee is what should be said about the approaches which have been received. Mr Newton wants to answer an arranged Parliamentary Question before he sees the Trade and Industry Select Committee on 7 June. The Chief Secretary wants to reject the bids now; Mr Newton wants BS to assess them and consider the outcome later before the end of June. The major judgement for the Committee will be whether to adopt the first course, so as to avoid raising false expectations and suggesting any weakening in the Government's stance, or the second, so as to avoid rejecting bids without even considering them, and to put off the final decision by a month.

10. You will probably wish the Committee to take a clear-cut decision now. In principle, compromises might be possible. For instance, E(A) might decide now that continuation of shipbuilding at Sunderland was most unlikely to be acceptable but let the evaluation take place before a final decision was announced. The difficulty with this is that BS might nonetheless recommend acceptance of one of the bids. Mr Newton's paper says that there is genuine doubt about whether either bidder would meet the Government's criteria (para 9). But his letter of 26 May said that "there is every chance this time that one of the bidders will satisfy our criteria". This suggests that if the bids are to be assessed the Government must be prepared for one of them to be accepted if it passes the tests.

HANDLING

11. You will wish to ask the Chancellor of the Duchy of Lancaster to introduce his paper. The Chief Secretary, Treasury is the other main protagonist. We have invited a Foreign Office Minister to attend, to give views on handling the European



Commission. The Secretary of State for Scotland would have an interest if Commission approval for the shipbuilding package as a whole, for example sale of Clarke Kincaid, were to be threatened.

RJW

R T J WILSON
Cabinet Office

June 2, 1989

CONQUEROR

*file*PRIME MINISTER

MEETING OF E(A): TUESDAY, 6 JUNE

You saw last weekend the recent exchanges between Tony Newton and John Major on North East Shipbuilders Limited (NESL).

You commented then that you thought John Major had the stronger arguments; and that if one aspect of the earlier deal was re-opened, all aspects would need to be looked at again with possibly disastrous consequences for Sunderland. But you said that, if Tony Newton wanted a meeting of E(A), you would have one.

We discussed this with Tony Newton's Office earlier in the week, and he has come back to say he would like a meeting. This has therefore been arranged for Tuesday.

You are already familiar with the main issues, but you may like to glance over the weekend at the latest papers. These are:

- Flag A Formal E(A) paper by Tony Newton summarising the arguments and attaching at an annex the earlier exchanges of letters
- Flag B Cabinet Office brief
- Flag C Note by George Guise which amplifies the information in Tony Newton's paper about the German and Greek consortia who are interested in purchasing NESL.

Rec.

PG

2 June, 1989.

PA

cc file
cc 2/0

Mr. Gray of

*E(A) he wants. Tues. 11:30
to come round the ~~PM~~
George Monger has fixed return.*

MR MORRIS

BRITISH SHIPBUILDERS

I put some papers into the Prime Minister over the weekend (attached) concerning the dispute between Tony Newton and John Major on British Shipbuilders.

You will see from my covering minute below that the Prime Minister is siding with John Major, but is prepared to hold a meeting of E(A) if Tony Newton wants one. I read over to Linda Joyce in Tony Newton's office this afternoon the Prime Minister's manuscript comments. I told her that the ball was now in Mr Newton's court to decide whether or not to press for a meeting. She promised to come back tomorrow, and I suggested she had a word with you (in the hope that there is no need for me to come in!). I also said that, if he wanted a meeting, I thought we could find an hour next Tuesday morning - the keep free for me in the diary at 1130 was a contingency for that purpose.

If Newton decides he wants a meeting, could I ask you to liaise with the Cabinet Office (I think George Monger is in) to convene it next Tuesday. If Newton decides he does not fancy taking his chances in a meeting, we had better minute out the Prime Minister's comments in suitably diplomatic terms (I told Linda Joyce that we would not minute out until they came back to us tomorrow).

PR CC.

PAUL GRAY

30 May 1989

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the department for Enterprise

0 D *CPV*

The Rt. Hon. Tony Newton OBE, MP
Chancellor of the Duchy of Lancaster and
Minister of Trade and Industry

CONFIDENTIAL

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26 May 1989

John G. ...

BRITISH SHIPBUILDERS: NORTH EAST SHIPBUILDERS LIMITED (NESL)

We met on 24 May to discuss what the Government's position should be towards the expressions of interest which have emerged in purchasing the assets at NESL for the purposes of shipbuilding. Since we could not agree, we undertook to set out our views for colleagues, as a basis if necessary for collective discussion.

This letter therefore amplifies the arguments set out in my earlier letters of 19 and 24 May as to why we should be prepared to allow BS to negotiate with the two prospective purchasers who have emerged and, if I am satisfied that at least one of the bids is viable, to allow a sale to go ahead. Decisions are needed quickly, because there is otherwise a real risk that both bidders will reach the conclusion that we are merely prevaricating: this would have damaging consequences, as I explain below.

The essence of my case is as follows. I made clear last December, following my announcement of the closure of NESL, that none of the investment would be disturbed until 30 June and that we would consider any serious offers to purchase the yards, provided that this did not prejudice the aid package which the Commission had approved for BS as a whole. At that stage,

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needless to say, neither I nor anyone else expected serious offers to come forward to restart shipbuilding: we had after all just failed after considerable effort to find any acceptable bidders. But there were a number of engineering and shiprepair possibilities which might have borne fruit.

We now, as you know, have two bidders of undoubted financial strength who have expressed strong interest in building ships in Sunderland. I gave details of the parties in my earlier letters. Both own and operate substantial fleets and are thus in a position to place orders. One, the Greek Shipping Consortium, has already put in an initial cash offer of £7.5m. The gross estimated break up value of the yard is £8.2m, but taking account of costs associated with a piecemeal sale over a long period, BS estimate that net receipts would be well below what the Greeks have offered. They and the German partnership, who have offered to match whatever the Greeks bid, are precisely the sort of bidders for which we looked in vain last Autumn. Their appearance now is a reflection of the significant change which has taken place in market conditions since then, on which I say more below. They are sufficiently confident of the market to be prepared to go ahead without Intervention Fund support.

We have taken exceptional steps, including the creation of an Enterprise Zone, to attract business and jobs to Sunderland. We now have the prospect of a significant number of engineering jobs, possibly building up to 800 over the next two years. If such a prospect had emerged in any other industrial sector we would have welcomed it with open arms. The issue as I see it is what justification we have for rejecting it simply because it involves shipbuilding.

When we met, you put forward a number of arguments for doing so. Let me deal with each in turn:

a. The Market

You argued that, given the cyclical nature of the shipbuilding business, these jobs could never be regarded as long term, and it was better for Sunderland to make a completely fresh start. I acknowledged that I myself used similar language in defending our earlier decision to close NESL. But this was in circumstances where no bid which looked capable of being acceptable had emerged, and I was being urged to find some way of propping up the yards at public expense in the hope that something would turn up. Those circumstances have simply changed; and in any case, there is certainly no

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prospect of Sunderland returning to the degree of dependence on shipbuilding which existed prior to the closure, let alone in earlier years. In other cases, such as Govan we have accepted that private sector management should be allowed the opportunity to make a go of shipbuilding. As for the state of the market, the Greeks and their shipbuilding advisers have left me in no doubt that they now see an early and sustained recovery in the smaller size of merchant ships which NESL is particularly suited to build. They are prepared to back this judgement with hard cash. The Germans take a similar view.

Independent shipbuilding research organisations have since last year been forecasting that a broad balance between shipbuilding and shipping capacity would be sustained from the mid 1990s due to the large numbers of ships reaching the end of their life, and certain structural changes in the market, including the large volume of shipbuilding capacity which has been scrapped. The recovery in the type of ship which NESL builds has begun earlier than expected, but its reality can be judged by the fact that two and a half times the volume of this kind of shipping was ordered in the first quarter of 1989 compared with the similar period a year earlier, and that it is now becoming difficult to find berths for these types of ship - which is one reason why bidders are interested in the facilities at NESL, although their main motivation is to insure themselves against high ship prices in future. In any other sector we would accept that commercial interests prepared to risk their own capital and effort should not readily have their market assessment second guessed. In this case we shall of course be looking critically at the viability of the proposals taking account of likely future work load. If they are not adequate, I shall refuse to accept the bids, as I did before.

(b) Government subsidy

You argued that, even if purchasers were prepared in present circumstances to risk shipbuilding without access to the Intervention Fund, they would exert irresistible pressure on us for IF subsidy if market conditions turned down. My answer to this is that we would make absolutely clear to any purchaser that under no circumstances would IF be available; and that our record in resisting subsequent pressure for IF from privatised yards demonstrates that such pressure can be withstood, even where the

consequences are serious, as they have been at Swan Hunter and Scott Lithgow. A prospective purchaser would know very well that for us to give way in one case would open the floodgates to all the others, and that we would for that reason never bow to such pressure.

Your other objections seem to me to relate not to the viability of the proposals themselves but the problems we may create for ourselves in permitting shipbuilding when we had earlier decided to close NESL:

(c) The package of remedial measures

I recognise that you feel strongly that you only agreed to the designation of an Enterprise Zone and other remedial measures on the basis that NESL was to close. The new factories will not require extra funds for EIEC, and the cost of the rest of the package broadly equates with the IF the yards would have needed. That IF will not be available to the new owners. The EZ package was clearly exceptional. In the circumstances colleagues agreed that it was right; and having announced the Zone we cannot now in my view retreat from that, if only because there would still be a very large drop in shipbuilding employment and the need to stimulate new employment remains. Nevertheless I accept that if the bids are accepted we should explore the scope to reduce the benefits in the remedial package: that part of NESL within the EZ should be removed from it (equivalent to 30% of the Zone); and it might also be possible to make some reduction in the retraining and local enterprise expenditure being provided through BS.

(d) The European Commission

You were concerned that the Commission regarded the closure of NESL as a condition of their approval for the sales of Appledore and Clark Kincaid and would extract some price for its reopening. UKREP's advice is that the Commission would be unlikely to let their views on any approach I made affect their handling of other state aid cases such as Harlands or Shorts. On the BS case itself, their concerns should be mitigated by the fact that subsidy counted against the sixth directive would not be involved, and if a possible purchaser were to give assurances that the Pallion Yard would not be reopened for five years (equivalent to closure in Commission eyes). But the only way to test whether this would suffice would be to make an informal approach myself to Leon Brittan. I would then

need to judge whether any conditions the Commission sought to apply prejudiced the other BS disposals, which I have repeatedly said I will not do. I understand that re-opening shipbuilding would not affect the Commission's attitude to the EZ, since they regard it as justified by conditions on Tyneside, regardless of the position at NESL.

Precedent

(e) Finally, you argued that the precedent set by allowing the reopening of a closed yard would undermine the Government's position if similar decisions had to be taken in future, either in relation to a privatised NESL or other state owned assets. On the first point, there is ample evidence both in shipbuilding and elsewhere that decisions taken by private management to cutback or close privatised concerns raise nothing like the political problems of decisions taken or endorsed by Government to close publicly owned undertakings. Nor do I believe NESL sets an undesirable precedent for future public sector closures. I made clear at the time of the closure that we remained interested in disposing of the assets on a commercial basis providing the business involved was viable. In agreeing to sell we would not be going beyond what is already our position.

As I understand it, your preferred course would be either to tell BS to break off contact with possible purchasers, or alternatively to go through some kind of bidding process with a view to concluding that neither of the bids likely to be made is viable. I am bound to say that either variant looks deeply unattractive. Both would call in question - to put it mildly - our good faith in everything we said and did to find a way forward for NESL over many months, and would be widely interpreted in the North East as a clear indication that we had simply been determined to close the yards come what may. Contrary to the position last autumn, when even the most ardent opponents of closure knew in their hearts that the bids we had received at that time were unacceptable, there is every chance this time that one of the bidders will satisfy our criteria, and we will be unable credibly to sustain an argument that the interest now being expressed lacks any prospect of viability, especially if (as seems likely) the rebuffed bidders then put work into overseas yards.



the department for Enterprise

The Greeks, who have repair work for this summer, are becoming increasingly irritated at what they regard as stalling on BS' part. They will be visiting Sunderland next week and can be expected to stoke up considerable media interest. Playing for time is not an option. We have to decide now, not that BS should accept one of the bids, but whether there should be a genuine evaluation leading to a sale if they are satisfactory. This is the course I firmly recommend.

I am copying this to recipients of our earlier correspondence.

TONY NEWTON

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PRIME MINISTER

BRITISH SHIPBUILDERS

Last weekend you saw a note from Tony Newton to John Major (flag A) indicating that two groups of shipbuilders - one Greek, one German - had now expressed interest in taking over North East Shipbuilders Limited (NESL). Tony Newton wanted to consider these proposals, rather than proceeding with the earlier plan for closure of NESL.

During the course of this week, there have been heated exchanges between Tony Newton and John Major about this, and I now attach some further papers. These are:

Flag B - initial response from John Major

Flag C - record of a meeting between John Major and Tony Newton held on Wednesday. (You only need to glance at paragraphs 2-10 on NESL; the later material on Ferguson relates to a separate dispute that is now being sorted out between the Treasury and DTI).

Flag D - further detailed letter from Tony Newton which seeks to answer point by point the issues that John Major has raised;

Flag E - short note by George Guise. Although George wrote this earlier in the week before some of the later papers were available, his views remain as set out there.

John Major has yet to respond to the latest Tony Newton note at flag D. But I understand that he is likely to continue strongly to resist Tony Newton's proposals, and there is little prospect of them reaching agreement bilaterally. So you may like to have a look at these latest papers over the weekend and consider how the issue might be resolved.

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I think there are four key points:

- the politics of an announcement that NESL might be reprieved. Tony Newton says it is politically impossible not to consider the new approaches that could save the yard. John Major sees such a move as a major act of political weakness.
- should the assertion by the Greek and Germans that they would require no subsidy be believed? Tony Newton thinks it should; John Major is highly sceptical and thinks that in the longer run the Government will be pressed for assistance.
- should the earlier package of assistance for Sunderland, put together when it seemed NESL would have to close, be reconsidered? John Major argues strongly that it should; Tony Newton now seems to be accepting that there could be some degree of re-negotiation.
- would re-opening this put us in difficulties with the Commission, not only in relation to assistance for Sunderland, but also on other outside state aid issues, eg Shorts and Harland and Wolff? Again, Tony Newton and John Major take opposing views.

Yes - if NESL is to be reprieved the package is cancelled

You will see from George Guise's note at flag E that he considers there is force in the arguments on both sides. But he sees the first of the four points above, the political aspects, as the key.

~~Handwritten signature~~

I think there are three options:

- (i) to convene a meeting under your Chairmanship, which we could squeeze in on Tuesday 6 June. This could be either:
 - a full meeting of E(A), or
 - a smaller ad hoc group
- (ii) for you to intervene in support of Tony Newton, so aiming to resolve the dispute without the need for a meeting;
- (iii) for you to intervene in support of John Major, so again aiming to resolve the dispute without the need for a meeting.

Which option do you prefer?

Pls.

PAUL GRAY

26 May 1989

I think John Major has the argument.

You cannot do a deal like this and then go back on it. If we reopen one thing we reopen all with what I think would be disastrous consequences for Sunderland. But if Tony Newton wants a meeting of E(A) I will have one

PM2AQN

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BRITISH SHIPBUILDERS: NESL AND FERGUSON

Note of a meeting held in the Chief Secretary's office
H M Treasury, on 24 May 1989. Those present:

Chief Secretary
Mr Guy
Mr Wanless

Chancellor of the Duchy of Lancaster
Mr Coates
Mr Alty

The Chief Secretary thanked the Chancellor of the Duchy for his letters of 19 May and 24 May. He had also seen the Secretary of State for Scotland's letters of 18 May and 23 May. Although he had suggested it might be possible presentationally to link the NESL and Ferguson issues, any connection should only be made after separate decisions had been taken on merits on each case. The Chancellor strongly agreed with this approach.

NESL

2. The Chancellor said that he had restated his view in his letter of 24 May. He thought the crucial point to answer was on what basis the Government could decline an offer for the yards at or above the asset value for the purpose of building ships there. The impression was that the Treasury was happy to see any business except shipbuilding establish itself in the area. The Chief Secretary asked what the Chancellor meant in the fourth paragraph of his letter when he referred to offers being equivalent to the value of the assets without any special form of Government support. The Chancellor said this meant without all forms of support specifically or directly related to shipbuilding and almost certainly without support for Southwick within the Enterprise Zone (EZ). The Chief Secretary said that he could not contemplate inclusion of Southwick in the EZ if shipbuilding continued there. The Chancellor said that the Greeks had been told that it was highly unlikely that the yard could remain in the EZ. However, he saw no basis on which they could be deprived of generalised support available to any similar manufacturer through export credit facilities or the Home Shipbuilding Credit Guarantee Scheme. The Chief Secretary observed that that scheme was in effect a specific subsidy to UK shipbuilding.

3. The Chief Secretary queried the reference in the Chancellor's latest letter to a marked change in the market for ships. He could not accept this on the basis of one quarter's figures that this was anything more than a transitory blip and he was inclined to believe that in the medium term Sunderland would not be able to compete on the world market. This was clearly the view last year when difficult decisions had been taken to close the yard and offer an expensive remedial package. Foreign owners might possibly establish themselves with no initial recourse to subsidy. But he foresaw the time, in the near future, when the business would be marginal again. Then there would be pressure for Government support all over again. Politically, these would probably be almost impossible to resist. The Chief Secretary said that despite an agreed policy of no more EZs he had agreed exceptionally to a support package on the Wear, only on the basis that there was no long-term future for shipbuilding at NESL. The Chancellor had consistently refuted claims that a market upturn could offer any hope to NESL. He had done so in the House only a few months ago. There would be presentational difficulties in reversing this recent market judgement. It would also set an extremely awkward precedent for the future. Whenever the Government contemplated any closure, opposition would always quote the NESL case. They would claim that, like Bunter's postal order something would always turn up. He did not accept that such a fundamental change in the shipbuilding industry had occurred.

4. The Chief Secretary said that the position with the EC also worried him. He thought that the Commission had allowed a number of deals to resurrect shipbuilding elsewhere in the UK on the basis that the NESL yards would close. Although the EC might be powerless to prevent unsubsidised shipbuilding there was a danger that they might extract a price either there or perhaps in other cases where their cooperation was needed. The Chief Secretary thought that these generic arguments were a strong enough basis on which to close the yards for good without considering the details of any bids

5. The Chancellor said that the situation was very different now from when he announced closure at NESL on 7 December. For the first time he had received sustainable bids from initial viability bidders. The Chief Secretary said that even if he accepted the viability of any bid this had to be balanced against whether this would remain the case; whether the investment would provide long term employment given the nature of the shipbuilding market; and whether the long-term future of Sunderland could not better be served by establishing a diversity of sustainable new business in the EZ. All these doubts led him to conclude that for Sunderland's sake it was right to bite the bullet now.

6. The Chancellor said there was an upturn in the shipbuilding industry. The Japanese had been retrenching. The Chief Secretary said one might argue that this was because they saw that shipbuilding with higher capacity was not profitable in the medium term. Low cost capacity remained in the Far East at levels which businesses there thought was viable in the global market. Mr Coates said he stood by the gloomy descriptions of the market which his Minister had made, though he stressed that the downside had been emphasised for presentational reasons. However, the combination of a number of structural factors led him to conclude that the future was now looking more bright for manufacturers. In particular, many ships which were built around 20 years ago were now due to be replaced, leading to a market upturn. Mr Guy expressed concern that this model of the shipping industry was exactly the one which had supported the conclusion that shipbuilding in Sunderland was not viable. In explaining the closure of NESL the Government had said that despite this expected upturn they saw no viable future for shipbuilding at NESL. Mr Coates said the Government had focussed on BS and the losses they had made on top of subsidy. They had concluded that with better management and changes in working practices it ought to be possible to build ships there and be competitive in international markets: but it was impossible now to turn round the performance of BS itself. Mr Guy said there had been more to our arguments than this. We had told people that we had considered the state of the market and concluded that, even in the event of

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an upturn, we thought it impossible now to build ships competitively at NESL and on this basis the yards had to close. Mr Coates said that Ministers' first approach in 1987 had been to say that they could not see a future for the industry because of the losses it was incurring. Govan had been kept open with generous subsidies. The last Chancellor had wanted to avoid such expenditure so he appointed John Lister who said the best that the yard could achieve was to break even. But Kvaerner had said they could turn the yard round, so the Government developed its privatisation policy to try and dispose of the yards. Mr Coates saw the crucial question as whether bidders could be found who were prepared to pay for the yards.

7. The Chief Secretary said that he was grateful for this background but it did not fully answer his concerns. What would the EC view be of the continued shipbuilding at Sunderland? Would the Greeks or Germans ask for Intervention Fund support? Could we resist it? Were the bids so good that the Chancellor preferred them to the enterprise zone?

8. Mr Coates said that the EC had no difficulty with Govan. As to later disposals at the end of 1988, the UK had presented a package showing total state aid to BS on the basis of full NESL closure. Undoubtedly closure of NESL represented a political advantage to the Commission's policies. But it was unclear how much of the shipbuilding capacity they would be content to see continue without Intervention Fund support. Neither bidder would be building ships in the Pallion yard for five years, so there was a degree of restructuring. He therefore saw a case for the Commission to agree to Southwick only continuing. The Chief Secretary said he thought the Commission would say that they had agreed state aid on the basis that all NESL capacity was to be eliminated. To renotify NESL now would be considered an act of very bad faith. Even if Sir Leon Brittan was accommodating the deal would hang there for use against us on future occasions.

9. On whether he could realistically resist future claims for Intervention Fund support the Chancellor said that the Scott Lithgow and Ailsa yards had been sold without access to the Fund. They and others were now pressing for a return to support and he had resisted. The Chief Secretary said that these cases were materially different because they were only making military ships.

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The Chancellor said that - leaving aside the removal of Southwick from the zone - he did not see a viable trade off between the whole EZ and continued shipbuilding at NESL. The Chief Secretary said that it had only been closure of the yards that had persuaded the Government to agree the support package. The Chancellor said that a choice between selling the yards or conceding the entire EZ, would be impossible. At least half the NESL workforce would be unaffected by the sale. The Greeks would provide 800 to 1,000 jobs over an uncertain timescale. There was no indication yet of the precise size of operation envisaged by the Germans.

10. The Chancellor thought that there were presentational difficulties whether he considered these bids further or not. But he thought that the situation had altered since December because he had credible buyers and the Government would not have to provide money to keep the yards open. The Chief Secretary did not accept this distinction. He thought it highly likely that any buyer would soon be at the Government's door requesting support to sustain employment and we would be faced once again with the familiar subsidy/closure arguments. He noted that he and the Chancellor disagreed over the politics and presentational aspects of the issue; over whether continued shipbuilding was in Sunderland's interest; over their view of the shipping market; and the extent to which the Government may or may not be able to resist future claims for support. No agreed conclusions were likely in the time available; they would need to consider this further.

FERGUSON

11. The Chief Secretary noted that last time the workers at Ferguson had been presented with a bid for the yard it had been rejected by 277 votes to 3. He thought they valued their closure bonuses too much to keep the yards open. The proposition seemed to be that HLD were now providing such an attractive package that they could turn this vote around. As the Secretary of State for Scotland had noted, the attitude of the workforce was a critical factor.

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12. The Chancellor agreed. The Ailsa bid had been badly handled. He thought that Bill Scott, who was leading the HLD bid had more chance of success. Mr Coates said there was presentational advantage in letting the workforce consider the HLD package. If they turned it down, it would effectively be them who had closed the yard. The Chief Secretary asked how many more times they would be offered similar opportunities. We had told them last time that the Ailsa bid was their final chance to keep the yards open.

13. Mr Coates said that there was no work at Ferguson. Consequently if the HLD bid failed, the yard could be stripped the very next day. The Chancellor said that this was to be the very last chance which the workforce were to have. The Chief Secretary thought that phrase had a familiar ring.

14. The Chief Secretary said that he would like to discuss Ferguson with the Secretary of State for Scotland. However, he queried whether it would take four weeks to ballot the workforce Mr Coates thought a decision could be reached in 3 weeks at the outside. He would provide the Chief Secretary with an estimate of the cost of keeping the yard open for this time. The Chief Secretary stressed that under no circumstances could he contemplate the Ferguson yard being included in an Enterprise Zone.

PW.

H M Treasury
26 May 1989

PETER WANLESS
Assistant Private Secretary

Distribution
Those present

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cc/b.

the department for Enterprise

The Rt. Hon. Tony Newton OBE, MP
Chancellor of the Duchy of Lancaster and
Minister of Trade and Industry

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Your ref
Date

215 5147

24 May 1989

Dear Chief Secretary

BRITISH SHIPBUILDERS

allaen

I am naturally disappointed by your letter of 22 May in response to the proposals I have made about NESL and Ferguson.

NESL

You argue that the politics of seeking to progress new bids for NESL would be wrong against the background of the decisions we reached last year. I have to say I believe that the political damage would be greater by far if we decided not to proceed.

We have already been criticised for applying double standards to the North East in comparison with Harland and Wolff. We have answered this by saying that we received no bids for NESL from groups with the industry experience and financial substance of Mr Olsen. Therefore the question of the generosity of support did not arise.

We now have two offers, totally unexpected and unsolicited, from exactly the kind of people we said we were looking for last year, looking likely to pay what the assets are worth without any special form of Government support.

What has happened is a marked change in the market for ships of the kind these yards can build. Two and half times the volume of this kind of shipping was ordered worldwide in the first quarter of this year in comparison with a year earlier, the backdrop to our previous disposal exercise. Brokers are unable to find berths for early delivery for ships of this size.

AC
SBLABM



The crux, as you point out, is that this would be shipbuilding without Intervention Fund assistance. It would be my intention in announcing the opening of negotiations with either the Greeks or their German counterparts to say that there would be no question of this kind of support now or later. The risk would be theirs. The Germans have now also confirmed they would proceed without help.

So far as subsequent requests for aid are concerned, we have successfully held the line against pressure for renewed IF support at several of the yards previously sold without it. I have already myself made absolutely clear to the Greeks that there would be no question of going back

You point out that we made provision to encourage diversification of the economy in Sunderland. Considerable retraining and diversification will remain necessary even if we were to accept one of the proposals for NESL. But in our efforts to attract new business to the area, I cannot see any logic in stating that new activity is welcome provided it is not shipbuilding. Just as the Government is not in the business of picking industrial winners, neither is it in the business of deciding that certain commercial activities are not permitted.

You talk of your willingness to allow previous BS disposals in the knowledge that NESL would close. That is not my recollection of either the Govan or Appledore shipyards disposals, nor of other disposals made since, although you correctly recall exchanges about Ferguson when Clark Kincaid was sold.

I must therefore ask you to review these arguments and reconsider your position on NESL.

Ferguson

You said you were prepared to discuss further the Ferguson disposal. In view of the urgency, our offices have arranged a meeting later today on this. But it follows from what I said above on NESL that I could not accept that a decision on Ferguson should be conditional on my agreeing to your view on NESL. The two cases must be considered on their merits.

I am copying this letter to the Prime Minister, Sir Geoffrey Howe, Norman Fowler, Tom King, Nicholas Ridley and Malcolm Rifkind enclosing copies of the earlier correspondence on Ferguson for those of our colleagues who were not included in the original circulation, and a copy of my letter about NESL to Malcolm Rifkind.

Yours Sincerely
John Atty

TONY NEWTON

*(approved by the Chancellor
and signed in his absence)*

23 May 1989

BRITISH SHIPBUILDERS - NESL

DTI and the Treasury have taken extreme positions. The former argue that the market has now turned and shipbuilding will be in the ascendent and therefore we must respond to any glimmer of hope which could reverse the closure of NESL. By contrast, the Treasury argue that the decision has already been made on solid economic foundations, to close Sunderland and get the government out of state supported shipbuilding. Of the two letters, the Treasury's is the more persuasive. ✓

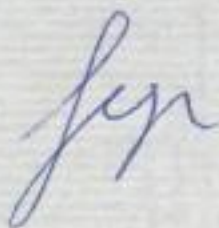
Nevertheless, the whole concept of an enterprise zone is that industry should be encouraged to locate there. Why regard shipbuilding differently from other industries? Newton believes that he has buyers for the yard who will build ships without state support. If this contention withstands rigorous examination, then it might be better to have Greeks or Germans building ships in Sunderland than an artificial conversion of the facilities for some other industry.

The Treasury's fear is that this will be read politically as a hasty government response to apparent short-term strength in the shipbuilding market leading to a policy reversal of enormous and adverse political consequence. If that argument prevails then Newton should not be encouraged to proceed. However a purely commercial view must be that the acceptability of private shipbuilding in Sunderland should be no different from any other industry.

Provided that there are no special financial arrangements such as intervention funding or special ECGD arrangements, Newton should be encouraged to negotiate a concrete

arrangement with either Greeks, Germans or anyone else with ready money for the sale of the shipyard.

HMG must make it perfectly clear that there is no question of backtracking and that British shipbuilders is not reopening anything. Its operations have been closed in Sunderland and remain so. Alternative owners may make whatever financial arrangements are acceptable to their shareholders.

A handwritten signature in blue ink, appearing to read 'G. Guise', is centered on the page.

GEORGE GUISE

CONFIDENTIAL



B B

CCP4

Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon Tony Newton OBE MP
Chancellor of the Duchy of Lancaster
Department of Trade and Industry
1 - 19 Victoria Street
London
SW1H 0ET

22nd May 1989

Dear Tony,

BRITISH SHIPBUILDERS: NESL

will request is required
Your letter of 19 May about the future of the British Shipbuilders yards in Sunderland causes me grave concern.

I had thought that we had agreed that shipbuilding on the NESL sites would inevitably and irretrievably conclude when the rump of the Danish ferries order was complete. This is certainly the understanding on which I agreed to extremely generous remedial measures for the area. It is also the understanding on which I have agreed to a series of unsatisfactory financial deals to save other yards from closure. I had thought that the point of that was to ease your burden in presenting the unavoidable bad news on NESL and the Ferguson yard in Scotland, on which you have written to me separately. You would not, I am sure, have put these other cases to me as you did if you had had any other expectation.

We always knew that this was going to be difficult, and I do not underestimate the problems you have faced. But NESL is virtually shut already and there is no merit whatsoever either presentationally or financially in trying to reopen the site and the issues now. Rather than try to argue the European Commission into agreeing to a resurrection, my view is that you should simply remind them that the elimination of NESL capacity was the price they sought for agreeing to exceptional state aid in the other cases.

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Financially, it is clear that disposal to the German interests would be adverse, given their expectation of state aids. The Greeks are in fact offering less for the site than its value, but even if they were to improve their offer you would need to believe that they would not be receiving state aid in the future. I note that they are not 'insisting' on Intervention Fund support at this stage. But I have no doubt that whatever the basis for their arrival, they would soon be holding us to ransom publicly for maximum state aid. They would be foolish not to. And when they did it would be difficult to refuse. This is a slippery slope we should avoid.

Aside from the financial aspects, I find the presentational implications of your proposal alarming. The world at large thinks that shipbuilding at NESL is over. We have introduced a range of regeneration and retraining measures out of all proportion to what we have done in other cases where jobs have been lost due to essential restructuring, which would be quite inappropriate if the yards were to stay open. We have emphasised the benefits of a future away from the decline of the traditional local manufacturing base. Almost all the men are now redundant and almost all the site is now on care and maintenance.

Into all this you propose now to announce that Sunderland has a future building ships after all, and that the men who are being retrained should go back into the yards which we have just shut as a British concern in a blaze of adverse publicity and with great social upheaval to work for foreign interests instead. I do not know how you would then resist calls for state support from the new owners unless you were prepared to go through the whole exercise again. Moreover would not this volte face be used against us whenever, in the future, we again sought to close unprofitable enterprises.

This is all unnecessary. I believe strongly that the yards should be allowed finally to close.

I am sending copies of this letter to the Prime Minister, Geoffrey Howe, Norman Fowler, Tom King, Nicholas Ridley and Sir Robin Butler.

Yours Ever,
John
JOHN MAJOR

CONFIDENTIAL





NBPm

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26/5

Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon Tony Newton OBE MP
Chancellor of the Duchy of Lancaster
Department of Trade and Industry
1 - 19 Victoria Street
London
SW1H 0ET

22nd May 1989

Dear Tony,

BRITISH SHIPBUILDERS: FERGUSON YARD

Thank you for your letter of 17 May. I have also seen Malcolm Rifkind's views as recorded in his letter of 18 May. I have carefully considered the arguments, but I am unable to agree with your conclusions.

There would be no point in delaying a decision on the future of Ferguson unless there were a reasonable prospect of a satisfactory disposal at the end of it. I would be very surprised indeed if you felt that you would be able to recommend the disposal of the yard on the sort of terms you describe. Looking at the position of Ferguson on its merits there is, regrettably, no possible conclusion but that the yard should close immediately, and it should not be necessary for us to discuss this any further.

We have always known that it was extremely unlikely that a basis for disposal of Ferguson could be found within the agreed policy. It will come as no surprise to anyone familiar with the circumstances and history of the yard if it now closes. I do not imagine that this will be easy for you or Malcolm to handle, but it has been an inevitable decision for some time. I had it in mind when I agreed to the extraordinary deal on Clark Kincaid last year. At that time you rebuffed my suggestion that good news of the privatisation of Clark Kincaid should be linked with the bad news on Ferguson. You did however acknowledge that presentation of the likely closure of Ferguson would be eased by reference to the preservation of capacity and jobs at Govan and CK.

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The first bidding round for Ferguson proved conclusively that it could not be privatised within our policy quite apart from the sabotage from perfectly unacceptable employee demands. I agreed to the second round chiefly to assist your presentation, and on clear understanding that it was to be absolutely the last call.

I am of course willing to look with an open mind at the best of the new bids from the second round. But from what I see there is no acceptable basis for privatisation. Malcolm's calculations of tax and NI foregone seem conceptually wrong. Quite rightly they have not featured in previous cases and should not do so now. I sympathise with Malcolm's difficulties and I appreciate that it may appear to be a small amount of money which is at stake. But that is because it is a small yard. It is not a question of £230,000. The salient point is that the bidder is offering for the assets only 70 per cent of what they are worth; and this is before we begin to estimate future state aids, and it is on the dubious assumption that HLD will be able to do a deal with the workforce without worsening an already unacceptable deal.

As to presentation, I think it would be extremely unsafe to proceed on the basis that the financial relativities would be overlooked. It would quite properly be used to criticise you, (and me as well if I endorsed the deal). John Lister's advice gives you no comfort. He may be inviting you to override his commercial judgement, but he makes that commercial judgement very clear. It seems to me highly likely also that the immediate publicity would be more likely to focus on the 200 jobs lost than the 80 saved.

I am in any case far from persuaded that the preservation of a precarious shipbuilding activity is in the longer term interest of the area, whatever the cultural attachment to it may be. We have, as Malcolm mentions, installed an extraordinary range of regeneration measures in Inverclyde, and the preservation of yesterday's subsidised shipbuilding industry was very far from my mind when I agreed to them.

My conclusion is that the yard should be closed and its assets realised without delay. However, since reaching this conclusion I have seen your letter of 19 May about NESL to which I am replying separately. Although this does nothing to improve the individual position of Ferguson, it introduces a new and most unwelcome factor in presentation. If you feel it absolutely necessary to balance news of NESL's final closure with some good news, and if in the light of all the above you still saw some advantage in delaying a decision on Ferguson, I would be prepared, as absolutely the final concession in this BS saga, to discuss a basis on which we might do that. Otherwise I would see no point in discussing Ferguson any longer.

I am copying this letter to Malcom Rifkind.

Yours Ever,
John
JOHN MAJOR

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the department for Enterprise

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The Rt. Hon. Tony Newton OBE, MP
Chancellor of the Duchy of Lancaster and
Minister of Trade and Industry

Rt Hon John Major MP
Chief Secretary
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Direct line
Our ref
Your ref
Date

215 5147

19 May 1989

File Mark 2

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19/5

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Dear Chief Secretary,

BRITISH SHIPBUILDERS

When I announced the closure of North East Shipbuilders Limited last December I was pressed in the following emergency Debate to say what we intended about the future of the yards. Given that they are well equipped and represent considerable investment on behalf of the taxpayer, and because there was work to be completed on the Danish Ferries that would last until at least this month, I made an undertaking that none of the investment would be disturbed until at least 30 June.

Two groups of shipowners have now approached British Shipbuilders with a view to taking over the yards. One, a consortium of Greek shipowners which have retained the London Shipbrokers Clarksons to act on their behalf, have already made a cash offer for the yards of £7.5m, which is very close to British Shipbuilders property adviser's valuation of the yards and their plant and equipment on a break-up basis, and have done so without insisting on Intervention Fund support for new orders. The other interest is a partnership of private North German shipping companies. They appear more attached to initial help but there is no doubt of the financial resources available to both these groups.

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the department for Enterprise



I do not think it could be practical politics to set aside these approaches, especially in view of the growing evidence of an upturn in the shipbuilding market, as though they had not been received. The Greeks have already made their interest known in public. Provided I am satisfied that the substantiated plans of these two groups show a real commitment to a viable commercial operation, thus implying significant employment in Sunderland for at least a number of years, and Intervention Fund support is not necessary, I believe I should pursue them seriously with British Shipbuilders and be prepared to take either of them to the European Commission. Indeed, if entrepreneurs are prepared to embark on shipbuilding on an unsubsidised basis, it is difficult to see what arguments we could credibly use to justify preventing them.

Subject to your views and those of our colleagues to whom this letter is copied, and depending on the strength of the shipbuilding proposals as revealed in discussions between British Shipbuilders and the interested parties over the next two weeks, I intend to make a first approach to Sir Leon Brittan shortly. UKREP have advised that they do not believe such an approach would react adversely on the Commission's attitude to the parallel discussions about Harland and Wolff.

Plans are well ahead for the Sunderland Enterprise Zone. As it now stands, its designation includes one of the yards. Interests in Sunderland seem to accept that the re-emergence of shipbuilding should not be hindered but there is also concern to have the Zone in place as soon as possible. There are a number of options which will need examining over the next few weeks depending on these shipbuilding developments. This might include designating the yard but neutralising the benefits for a shipbuilding company, allowing the benefits subject to Commission agreement, or re-designating an equivalent area elsewhere.

I am copying this letter to the Prime Minister, to Sir Geoffrey Howe, Norman Fowler, Tom King, Nicholas Ridley and Sir Robin Butler.

Yours sincerely
Rosalind Cox

TONY NEWTON

[Approved by the Chancellor and
Signed in his absence]

SB1AAD





CHANCELLOR
18 MAY 1989
DUCHE DE LANCASTER

SCOTTISH OFFICE
WHITEHALL LONDON SW1A 2AG

COMMERCIAL - IN CONFIDENCE

Rt Hon John Major MP
Chief Secretary
HM Treasury
Parliament Street
LONDON
SW1

Allen

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48 May 1989

BRITISH SHIPBUILDERS: FERGUSON SHIPBUILDERS LIMITED

I have seen a copy of Tony Newton's letter to you of 17 May proposing that HLD should be designated preferred bidder for Fergusons. This proposal has my strong support.

It is difficult to arrive at precise calculations but it seems that disposal to HLD would exceed the break-up cost by a small amount, and future Shipbuilding Intervention Fund support to the yard would add to the net cost of disposal. But disposal offers savings of over £1m in indirect costs - lost tax and National Insurance contributions, along with income support - and these savings would go a long way towards offsetting the net disposal cost.

But my principal concern is that the Government should not be seen to be closing down a potentially viable business, with the loss of about 300 jobs in Inverclyde, when there is an immediate prospect for saving 80 of these, and the potential to increase employment further in the future. The closure would, incidentally, have the effect of closing down all that is left of the shipbuilding industry on the lower Clyde. As such it is likely to attract particularly strong public criticism. This after all is an area which is the subject of substantial Government investment aimed at reversing the area's economic decline. Our opponents will be quick to seize on the inconsistency of spending up to £45m on the area (£25m on the Enterprise Zone and £20m on the Inverclyde Initiative) plus Regional Selective Assistance, yet withholding the necessary one-off investment which would enable Fergusons to stay in business and secure jobs which already exist. And of course if the yard were to close, we would at once come under very strong pressure to extend the Enterprise Zone boundaries to include the shipyard site, with the expenditure consequences which that might entail.

We have looked at the credibility of HLD management, as well as the likely market prospects, before coming to a view on their potential viability. Both appear satisfactory. They have good prospects of

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winning orders for barge-mounted diesel engines for power generation, the facilities at Fergusons complementing those at Clark Kincaid, and there are potential orders for small vessels such as dredgers and tugs. They would, of course, also wish to compete for any orders from Caledonian MacBrayne; there is a prospect, in the light of the company's operating requirements, of bringing forward a vessel replacement. Of course, Fergusons would have to compete with other yards - but in the current market conditions they would be strong contenders.

In the circumstances I wholly support Tony Newton's proposal that British Shipbuilders should designate HLD as preferred bidder and that this should be done quickly. This will allow the company to test the attitude of the workforce and provide the opportunity for further clarification of their bid before present work runs out.

I am copying this letter to Tony Newton.

*Approved by Secretary
in his absence*

MALCOLM RIFKIND

Approved by the Secretary
of State and signed in his
absence

The Rt. Hon. Tony Newton OBE, MP
Chancellor of the Duchy of Lancaster and
Minister of Trade and Industry

CONFIDENTIAL

Rt Hon John Major MP
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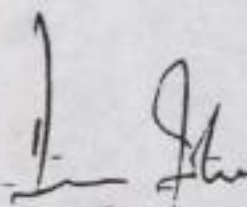
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Alison
Also
24/5

Direct line
Our ref
Your ref
Date

215 5147

17 May 1989

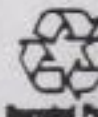


BRITISH SHIPBUILDERS

You will recall that you agreed to a new deadline for bids for Ferguson. On 21 April I was advised by the Chairman of British Shipbuilders that, as they stood, none of the new bids for Ferguson Shipbuilders Limited was sufficiently attractive on commercial grounds to allow him a clear recommendation that negotiations should open with a preferred bidder with a view to disposal. However, John Lister pointed out that he and his financial advisers agreed that the bid from the BLD Group, the buyout team that acquired the nearby Clark Kincaid engine business, could form the basis of a successful disposal. He suggested therefore that negotiations should be opened with BLD to explore options which might lead to a more satisfactory basis for disposal. He also said that if it were felt that the balance of considerations justified it, he would be prepared to negotiate a disposal to BLD.

In the meantime there have been further discussions with Apollo Engineering, another of the bidders, which made clear after Lister wrote that they might be in a position to increase their bid substantially. In the event Apollo bought another business and were not able to make a timely improvement for Ferguson.

CDLAAO



Recycled Paper

There have also been informal discussions with HLD as a result of which Lister and my officials have concluded that it is most unlikely that HLD could be in any position to improve their bid in a period likely to be acceptable to us beyond reaching agreement with the workforce on numbers, terms and conditions. To avoid further delay and local uncertainty I therefore conclude that we should address the future of the yard now on the merits of HLD's bid and the broader aspects of this disposal on which Malcolm Rifkind may care to comment.

HLD bid £570,000 for the assets of Ferguson. Whilst this was the highest bid, it is less than the net break-up proceeds of £800,000 forecast by the Corporation's property advisers. Disposal forecasts need to be treated with care but Lister felt that the gap between the forecast and HLD's bid was too wide to ignore.

No doubt mindful of difficulties between the Corporation's previous preferred bidder and the workforce, all the bidders save HLD required BS to make the whole workforce redundant. This the Corporation's Employee and Industrial Relations Director believes would result in pressure for a closure bonus on grounds of parity with other BS yards. - HLD is looking to retain a core workforce of 80 out of the present 290, thereby avoiding redundancy expenses and a closure bonus. But they have asked BS to contribute an equivalent sum to cover payments to buy-out redundancy terms as at Clark Kincaid and in support of under-recovered labour and overhead costs in early operations. Since work in the yard is virtually complete (the majority of the workforce is presently sub-contracted to Kvaerner Govan and Appledore), HLD's bid is therefore some £200,000 more expensive than closure before the question of Intervention Fund support is addressed.

HLD's bid envisages a reduction in the workforce to 80 with a view to building up again as and when work allows. The company would start with sub-contract engineering work of the kind already secured for Clark Kincaid. The local market in West Scotland for this kind of work is buoyant at present. HLD also envisage building unpowered barges to carry marine engines for power generation projects in Third World countries.

An urgency in our present decision is that HLD is in a position to sub-contract to Balfour Beatty for marine engines and barge work for a project in Jamaica for which Balfour Beatty believe they are front runners together with a Japanese concern. If HLD were in a position to offer a barge from Ferguson towards the overall bid, the terms of which are to be decided by Balfour Beatty on 29 May, that bid could be some £4m lower than at present given an expensive tender from another yard. But HLD

would only bid for the barge if they were preferred bidders for Ferguson by 23 May when their own decisions have to be taken. Otherwise they say they would not take the risk. If Balfour Beatty were successful, barge work at Ferguson would employ 100 people for a year and radically strengthen early prospects for the yard.

HLD recognises that the prospects of achieving early ship orders are limited. Under European Commission guidelines for subsidy calculation, redundancy costs in shipbuilding below the permanent workforce in a yard needed to build ships - here about 150 - are counted against capacity to receive Intervention Fund support during the Sixth Directive, which covers the period to the end of next year. The likelihood is that a very low percentage figure would result, making a ship order improbable for the next eighteen months or so unless the market continued to improve as radically as of late. Looking ahead, however, HLD are hopeful that their good relations with Caledonian MacBrayne will give rise to further work.

It is unfortunate that the development aid assisted order for Ferguson discussed in the last PES round should have gone to Germany since it would have represented 2 years work in the yard. In view of the EC position, I consider it unlikely that IF support at Ferguson would exceed more than £2m in 1990/91 and 1991/92 together with less thereafter. This is largely a matter for the 1989 PES round and will be covered in the PES bidding letter I know David Young expects to be sending in the next few days.

The major downside risk is that the employees at Ferguson will press for complete redundancy and a closure bonus. If they were to do so, I could no longer take the view that Lister should be invited to negotiate with HLD. So long as they do not, however, I consider that the clear balance of advantage is that we should authorise such a negotiation.

I therefore very much hope that you will agree to my placing a written answer along the attached lines preferably at the end of this week and at the latest on 26 May. The text deliberately refrains from defining a period within which agreement with the workforce should be reached. This is on Lister's advice about the handling of the National Unions. However, he and Scott have agreed that they would make clear that they would be looking for agreement within four weeks.

I am copying this letter to Malcolm Rifkind, whom I know is very concerned about the future of the yard.

TONY NEWTON

CDLAAO



PROPOSED PQ ANSWER ON THE DISPOSAL OF FERGUSON

I have today invited the Chairman of British Shipbuilders to open negotiations with the HLD Group Limited of Greenock as preferred bidder for the assets of the Corporation's shipbuilding subsidiary Ferguson Shipbuilders Limited at Port Glasgow. HLD's bid depends on their reaching an early and satisfactory agreement with the workforce. I should make it clear that, should this not prove possible, I could not be optimistic that there would be any other realistic prospect of achieving a successful sale.

CONFIDENTIAL



MINISTRY OF DEFENCE WHITEHALL LONDON SW1A2HB

TELEPHONE 01-218 9000

DIRECT DIALLING 01-218

MO 26/3/1L

26 April 1989

Pl. file. WBP

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26/4

Dear John.

TYPE 23 FRIGATES

Thank you for your letter of 24th April agreeing that we should seek tenders for the next batch of Type 23 frigate orders. Tim Sainsbury will make the appropriate announcement on Friday.

I have no difficulty with your proposal that our officials should continue discussions in the areas set out in your letter, on the understanding that these will take place within the framework of existing Government policy. In this connection, I was grateful for your acceptance that there can be no question of reopening the decision to retain an amphibious capability in the longer term.

I also agree that it would be useful if we were to explain to your officials our programme of work to inform future maritime equipment decisions. I am particularly anxious to avoid the sort of last-minute disagreements about requirements which we have had in connection with frigates and which we encountered at the time of the decision to seek tenders for the Aviation Support Ship.

I shall not comment in detail on all the other points in your letter, not all of which I necessarily accept. I would only say

The Rt Hon John Major MP

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that following the adjustments which I made in LTC 89, and for reasons which my officials have now explained to yours, I can assure you that the defence programme is properly aligned with the resource position agreed in PES 88 on the basis of the understandings reached between us at that time.

Finally, I note and accept your position that the 1981 commitment to retain a force of about 50 destroyers and frigates is not self-evidently right for all time. We need to recognise, however, that it was addressed collectively as recently as last year in formulating the Government's response to the Defence Committee report on the Surface Fleet and has regularly had to be reaffirmed to Parliament since then. I am sure you will accept that until that commitment is changed, which would inevitably be a matter on which I would need to consult OD colleagues collectively, we must continue to procure the ships and equipment required to support our existing policy as planned.

I am copying this letter to the Prime Minister, the other members of OD, the Chief Whip and to Sir Robin Butler.

Yours truly,
George

George Younger

CONFIDENTIAL
FM UKREP BRUSSELS
TO IMMEDIATE FCO
TELNO 1366
OF 261716Z APRIL 89

FRAME INDUSTRIAL
HARLAND AND WOLFF : MEETING WITH COMMISSION, 26 APRIL

SUMMARY

1. COMMISSION INSIST THAT OPERATING AID ELEMENTS IN THE HARLAND AND WOLFF (H AND W) PRIVATISATION PACKAGE MUST BE COUNTED AGAINST 1989-90 AID CEILINGS AND CONSEQUENTLY REDUCE HEADROOM FOR CONTRACT SUPPORT FOR MEBO/OLSEN'S NEW ORDERS (ESPECIALLY IF ALL CONTRACT AID HAS TO BE OFFERED IN 1989), ON THE GROUND OF PRESERVING THE INTEGRITY OF THE 6TH DIRECTIVE. BUT WELCOME FLEXIBILITY OVER HOW OPERATING AID SHOULD BE RECKONED.

DETAIL

2. MCDONNELL AND GREER (DED, NI) MET A COMMISSION TEAM LED BY PETERSEN (DG IV) TODAY TO DISCUSS A NON-PAPER INTENDED TO SERVE AS A BASIS FOR A FORMAL NOTIFICATION OF STATE AID ELEMENTS IN THE H AND W PRIVATISATION PACKAGE. PETERSEN'S APPROACH WAS FULLY CONSISTENT WITH THE COMMISSION'S LINE OR WORKING CONSTRUCTIVELY FOR CLEARANCE OF THE PACKAGE WITHOUT PREJUDICING THE PRINCIPLES OF THE 6TH SHIPBUILDING AID DIRECTIVE, BUT NONETHELESS LED TO A SIGNIFICANT RESTRICTION ON AID AVAILABLE FOR THE NEW ORDERS TO BE TAKEN BY THE MEBO/OLSEN CONSORTIUM ACQUIRING THE YARD. DED FEAR THIS COULD ENDANGER THE PRIVATISATION DEAL.

3. THE COMMISSION HAD NO MAJOR DIFFICULTIES WITH THE ACCOUNT OF AID GRANTED IN 1975-86, PRIOR TO THE INTRODUCTION OF THE 6TH DIRECTIVE. THEY WERE ALSO PREPARED TO ACCEPT THAT OPERATING AID IN EXCESS OF THE CEILING IN 1988 COULD BE OFFSET BY THE HEADROOM AVAILABLE IN 1987 (THOUGH DED EXPECTED TO BE ABLE TO ADJUST THE FIGURES TO RESPECT THE CEILING IN BOTH YEARS).

4. THEY HAD MORE DIFFICULTY WITH THE PROPOSITION THAT PART OF THE COMPENSATION FOR COSTS OVERRUNS ON THE SWOPS VESSEL IN 1987-89 SHOULD BE RECKONED AS RESTRUCTURING RATHER THAN OPERATING AID, AND WERE SCEPTICAL OVER THE ARGUMENT THAT EXCESS OVERHEADS RESULTING FROM CONSTRAINTS ON THE SPEED AT WHICH RESTRUCTURING AND REDUNDANCY PROGRAMMES COULD BE CARRIED OUT SHOULD NOT BE SEEN AS OPERATING AID: PREVIOUSLY THIS HAD ONLY BEEN DEEMED RELEVANT WHERE A YARD WAS

CLOSING, BUT THE PARTIAL CLOSURES PLANNED AT H AND W MIGHT HELP THE ARGUMENT. DED UNDERTOOK TO SUBMIT A COGENT CASE IN THE NOTIFICATION PRECISELY ACCOUNTING FOR AND JUSTIFYING THE TREATMENT OF EXCESS OVERHEADS AS RESTRUCTURING/CLOSURE COSTS. PETERSEN APPEARED PREPARED TO LOOK AT THIS SYMPATHETICALLY.

5. THE MAIN PROBLEM HOWEVER AROSE FROM THE TREATMENT OF THE AID ELEMENTS IN THE POUNDS 60M LOAN STOCK AND POUNDS 39M RECOURSE FACILITY TO BE PROVIDED TO MEB0/OLSEN, TOGETHER WITH THE ARRANGEMENT FOR DED TO BEAR A SHARE OF ANY FUTURE COST OVERRUNS ON SWOPS. THE COMMISSION WERE FIRM THAT ALTHOUGH THE BENEFITS OF THE FIRST TWO ITEMS WOULD EXTEND OVER A NUMBER OF YEARS, THE FULL NPV OF THE AID INVOLVED WOULD HAVE TO BE COUNTED IN THE FIRST 15 MONTHS FROM THE SALE OF THE YARD TO THE EXPIRY OF THE 6TH DIRECTIVE AT THE END OF 1990. SPREADING THE BENEFITS OVER ANY LONGER PERIOD WOULD BE OUTSIDE THE TERMS OF THE DIRECTIVE AND INEVITABLY INVOLVE THE OPENING OF AN ART 93(2) PROCEDURE, WITH POOR CHANCES OF SUCCESS. MOREOVER, THE WHOLE OF THE POTENTIAL COMMITMENT ON FUTURE SWOPS OVERRUNS WOULD HAVE TO COUNT AS OPERATING AID IN THE SAME PERIOD, SINCE AID OFFERS HAD TO BE ASSESSED ON THE BASIS OF THE WORST CASE OUTCOME. PETERSEN URGED THAT THE SWOPS COMMITMENT BE REDUCED AS FAR AS POSSIBLE. HE ALSO INDICATED THAT THE COMMISSION WOULD ALLOW ALL THE FLEXIBILITY IT COULD IN THE ASSESSMENT OF THE AID INTENSITY OF THE LOAN STOCK AND RECOURSE FACILITY (EG. BY EXCLUDING FUNDING FOR NAVAL WORK AND DIVERSIFICATION), PROVIDED AN ADEQUATE ACCOUNT COULD BE GIVEN OF HOW THE ASSESSMENT HAD BEEN ARRIVED AT.

6. NONETHELESS IT WAS EVIDENT THAT THE COMBINED EFFECT OF THE AID ELEMENTS IN THE PACKAGE WOULD BE TO REDUCE SUBSTANTIALLY THE HEADROOM UNDER THE CURRENT 26 PERCENT AID CEILING FOR CONTRACT SUPPORT TO THE CONSORTIUM'S NEW ORDERS, PARTICULARLY IN 1989: ON THE FIGURES PROVIDED BY DED, IT APPEARED THAT NO MORE THAN 6 PERCENT MIGHT BE AVAILABLE (THOUGH REASSESSMENT OF INTENSITIES ETC SHOULD INCREASE THIS TO SOME EXTENT). PETERSEN INSISTED FIRMLY THAT ALL THE AID OFFERED TO SECURE A CONTRACT HAD TO BE COUNTED IN THE YEAR IN WHICH THE CONTRACT WAS TAKEN, AND THAT ARTICLE 5 OF THE 6TH DIRECTIVE DID NOT (NOT) ALLOW CONTRACT AID PAYMENTS TO BE RECKONED AGAINST THE AID CEILING (AS A PERCENTAGE OF TURNOVER) APPLYING IN THE YEAR IN WHICH THEY WERE MADE. NOR COULD THE TURNOVER RESULTING FROM THE ORDERS BE BROUGHT FORWARD INTO THE YEAR IN WHICH THE OFFER WAS MADE. ANY DEVIATION FROM THESE PRINCIPLES WOULD MAKE THE 6TH DIRECTIVE WORTHLESS AS AN INSTRUMENT FOR CONTROLLING AID AND PROMOTING RESTRUCTURING - THE BASIS ON WHICH IT HAD BEEN DEFENDED IN GATT AND OECD. DED POINTED OUT THAT THE MEB0/OLSEN BID WAS BASED ON

THE EXPECTATION THAT THE FULL 26 PERCENT WOULD BE GIVEN AS CONTRACT AID FOR THE FIRST ORDERS: WITHOUT IT, THE PRIVATISATION DEAL COULD BE IN JEOPARDY.

7. IT WAS LEFT THAT DED WOULD FURTHER DEVELOP THE DRAFT NOTIFICATION TO INCLUDE INFORMATION ON A VARIETY OF POINTS IDENTIFIED BY THE COMMISSION, STRENGTHEN ARGUMENTATION AND ADJUST THE AID INTENSITY FIGURES TO TAKE FULL ADVANTAGE OF THE SCOPE IDENTIFIED FOR GREATER FLEXIBILITY. THE CURRENT TIMETABLE WAS THAT THEY WOULD NEED A PRELIMINARY INDICATION OF THE COMMISSION'S INTENTION TO APPROVE THE AID BY 15 JUNE.

8. COMMENT : IT LOOKS AS IF IT WILL NOW BE NECESSARY TO EXAMINE ALTERNATIVE APPROACHES TO CONTRACT AID, EG. BY DELAYING SOME NEW CONTRACTS UNTIL 1990 WHEN MORE HEADROOM IS AVAILABLE, OR BY INCREASING THE REGIONAL INVESTMENT AID OFFERED AS COMPENSATION.

HANNAY

YYYY

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*Die Minister
they continue to
squabble. But I
think this means
that the tenders can
go ahead.
COP
2/7/6*

Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon George Younger TD MP
Secretary of State for Defence
Ministry of Defence
Main Building
Whitehall
London
SW1A 2HB

26th April 1989

Dear George,

mb

TYPE 23 FRIGATES

Pop

Thank you for your letter of 13 April which I have considered carefully since it raises important points of procedure that go wider than the proposed frigate tender.

Turning first to the specific question of the frigates, you point out that inviting tenders does not commit the Government to ordering any particular numbers of ships. On this basis, I would be content for the tenders to be invited subject to the following points :

- (a) the defence programme is brought within the PES 88 settlement. This will need to be done before we consider orders for frigates this Autumn;
- (b) as a matter of urgency your officials provide mine with your department's analysis of the relative cost-effectiveness of amphibious assets. As I mention below, this material is relevant to forthcoming decisions on Fearless and Intrepid quite apart from frigate orders;
- (c) our officials agree before the Recess a programme of work to inform future decisions on the level and composition of maritime forces. The sort of issues this will need to cover include the balance between ASW and AAW in a replacement for the Type 42, the relative cost-effectiveness of mines and ships, the balance between weapons and platforms and the options available as the Aircraft Carriers and Sea Harrier come to the end of their useful lives;

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- (d) our officials complete by the Autumn the discussions you mentioned on peacetime Fleet utilisation.

I would like to comment also on a number of points in your letter. First, you say that you would meet the cost of a further batch of frigates within the provision agreed in PES 88. However, as I understand the position, the defence programme which has emerged from your recently completed long term costing (LTC 89) is presently showing substantial excesses in 1990-91 and 1991-92 over the firm three year PES settlement we agreed last Autumn. As part of that settlement you agreed to "take the necessary decision to ensure that, by the end of LTC 89, the defence programme is within the PES 88 settlement". Until this alignment has been clearly achieved, I do not think we can establish with certainty the affordability of individual components of your programme.

Second, you refer to your announcement in December 1986 to retain an amphibious capability in the longer term. There is, of course, no question of reopening that decision, although it was not cleared at the time with Treasury Ministers. The announcement does not, however, point to any particular level of investment in assets related to the amphibious capacity and I am sure you would agree that, as in other areas of expenditure, it is important that investment in this area should be guided by proper analysis of relative cost effectiveness and value for money.

The paper attached to your letter makes clear that support of the amphibious force is one of the principle wartime tasks of the destroyer/frigate force. I am also conscious that we may soon be facing other proposals for expenditure in this area involving the future of Fearless and Intrepid and the results of the tender for the Aviation Support Ship.

At present the Treasury has little understanding of your department's analysis of appropriate level of investment in this area. Your officials have told me the conclusions your department has reached on the basis of analysis in certain Chiefs of Staff papers. But unfortunately they have not been prepared to provide my officials with that analysis. I do think it is reasonable for the Treasury to be reluctant to subscribe to conclusions which are based on an analysis that has been refused to us.

Third, you emphasis the importance of the current policy of "about 50" frigates and destroyers. As I said in my letter of 6 July 1988, a force level set in 1981 cannot drive policy indefinitely and is not self evidently right for the 1990s and beyond. We need to be able to address, on the basis of an open flow of information between our departments, the future level and composition of our maritime forces. The comments in your letter about the scarcity of OA resources, and the timescales of analysis, suggest that our analytical requirements need to be planned well in advance of decisions.

I am copying this letter to the Prime Minister, the other members of OD, the Chief Whip and to Sir Robin Butler.

Yours Ever,
John Major
JOHN MAJOR



17/10

10 DOWNING STREET

Prime Minister

This seems a rather
 tiresome dispute.

The Government are
 committed to maintaining
 a force of "about 50"
 destroyers & frigates. There
 are good commercial
 & shipbuilding reasons for
 placing tenders now. The
 defence secretary is not
 asking for extra money,

only to spend his
programme in line
with agreed policy.
The Treasury seem
to be attempting a
Defence Review by
stealth.

Agree that the tenders
should go ahead?

Yes
///

CAP
14/4.
no



ccpc
[Redacted]

MINISTRY OF DEFENCE WHITEHALL LONDON SW1A 2HB

MO 26/3/1L

TELEPHONE 01-218 8000
DIRECT DIALING 01-218

13 April 1989

Dear John,

TYPE 23 FRIGATES

I am writing to seek your agreement to invite tenders from shipbuilders for an order for up to four Type 23 frigates to enter service between 1993 and 1995 to replace four 25 to 28 year old ships paying off at the end of their lives. We need to place the order by the end of this year if force levels are to be maintained; the tenders are due to be invited now. Our officials have been discussing the background to the order for some months, following our agreement last July that Treasury officials should be given a summary of relevant operational analysis in the maritime area and meet with the experts concerned (my letter to you of 18th July 1988 and your reply of 25th July refer). The attached note summarises the points that have been made and the policy background.

Your officials have not felt able to agree, on the basis of this evidence, that tenders should now be invited, but I am not willing to delay the tendering process until they are convinced. Our commitment to maintain a force of about 50 destroyers and frigates is one of the main planks of the Government's defence policy; it is my responsibility to provide the equipment to sustain it. In our response to last year's HCDC report on the surface fleet, we rejected their conclusion that we would maintain the "about 50" policy by running on older ships approaching the end of

The Rt Hon John Major MP

COVERING SECRET
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their useful lives. As well as being modern and much more capable, Type 23s are more economical to run than the ships they will replace. For example, they are about 30 per cent cheaper in manpower, which is an important element in our forward plans to reduce naval manpower, both saving money and helping to offset demographic pressures.

I understand that the basis for your officials' refusal to agree that tenders should be invited is that they wish to satisfy themselves that the Government's policy to reinforce Norway by an amphibious force, which requires 8 to 10 destroyers and frigates in support, is cost-effective; they wish further operational analysis in aspects of maritime warfare to be conducted; and they want to address the productivity of the Fleet.

So far as the future of our amphibious capability is concerned, this has been carefully and exhaustively considered by Defence Ministers in recent years, in the light, amongst other things, of the Falklands Campaign. The decision to retain an amphibious capability in the longer term was announced in December 1986; it has been reflected in subsequent Defence White Papers. I am not willing to see the decisions which have been taken and announced reopened in the context of frigate orders (and, therefore, see no need to make available to your officials, as they have requested, the Chiefs of Staff papers concerned). To give up this commitment would entail a decision of Defence Review proportions, which would be one which neither Parliament nor the country would understand; moreover, it would go completely against the approach we have been adopting to the defence programme and resources. Further, as can be seen from paragraphs 8-9 of the attached note, the case for about 50 destroyers and frigates does not depend critically upon the requirement to support the amphibious force. The fact is that the wartime tasks of the Fleet in a number of campaigns could justify a much larger destroyer/



much larger destroyer/frigate force than that which we currently provide. (Indeed, it might be argued that the "about 50" policy acts as a brake on the expectations of the relevant major NATO Commanders, as well as on those of our own supporters and the HCDC.)

On the question of further operational analysis, I am advised that the further studies proposed are not necessary and would not represent the best use of scarce OA assets; they would, in any case, take around 12 months to complete and would not therefore be available in the timescale for this decision.

I dealt with the question of peacetime productivity in my letter of 18th July. The essential point is that we size the Fleet in relation to wartime tasks. But I would, of course, be content for there to be further discussions between our officials on peacetime Fleet utilisation, on the understanding that they are not linked to this batch of orders.

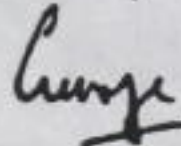
Against this background, and bearing in mind that inviting tenders does not commit the Government to ordering any particular number of ships, I hope you will feel able to agree that tenders should be invited now for the next batch of frigates. The "about 50" policy was an important part of our discussions on the defence programme and resources in PES 87 and 88; I would, of course, meet the cost of these ships within the provision agreed in PES 88. Parts of the warshipbuilding industry (especially Swan Hunter) will be critically underloaded by the time the first ship is due to start fabrication. Delay in inviting tenders could lead to the receipt of less competitive bids if, in the meantime, decisions were taken to lay off workers on the grounds that the prospect of new orders had receded. It could also cause renewed speculation and difficulty among our own supporters that our commitment to maintain a force of about 50 destroyers and frigates, which we are



about to reaffirm in the forthcoming Statement on the Defence Estimates, is not genuine.

I am copying this letter and the attachment to the Prime Minister, the other members of OD, the Chief Whip, and to Sir Robin Butler.

Yours truly,

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

George Younger

DESTROYER/FRIGATE NUMBERS AND THE TYPE 23 PROGRAMMEIntroduction

1. In his letter of 11 July 1988 giving agreement to an order for three Type 23 frigates, the Chief Secretary expressed concern that there appeared to be no substantive analysis of the cost-effectiveness of expenditure on frigates. He asked for a study to be undertaken by officials, to include an examination of the productivity of the Fleet in peacetime.

2. The Defence Secretary replied on 18 July explaining how the cost-effectiveness of destroyers and frigates had been judged and setting out the policy basis for the existing commitment to maintain a force of "about 50" ships. He agreed to make available to Treasury officials a summary of relevant operational analysis and for there to be discussion with the experts concerned. He explained why it was unnecessary to study peacetime Fleet productivity since this did not determine our force level requirements and was in any case demonstrably high.

Correspondence and discussions

3. Material was provided by the Ministry of Defence as follows:
 - a. On 13 July 1988, the Ministry passed to the Treasury a copy of its Conduct of Maritime Operations paper, which sets out the Royal Navy's strategy and tasks in war, and how they might be conducted with the forces planned to be available.

 - b. On 14 November 1988, the Ministry submitted a note summarising the insights derived from relevant operational analysis studies, together with a table showing the number of escorts suggested by these studies to be required to provide a marginally adequate to moderate capability. This indicated a requirement for about 60 ships.

c. On 22 December 1988, the Ministry submitted its plans for paying off and replacing destroyers and frigates over the period 1989 to 1999. Force levels were shown to remain between 47 and 49. The average age of escorts paying off was 23.8 years.

d. On 15 February 1989, at the Treasury's request, the Ministry submitted more detail in respect of the commitment to reinforce Norway by an amphibious force, support of which is one of the principal wartime tasks for the destroyer/frigate force, together with a note summarising the insights obtained from operational analysis of the relative effectiveness of frigates and naval mines.

Policy Background

4. The Government's commitment to maintain a force of about 50 destroyers and frigates derives from the 1981 Defence Review (Cmd 8288, The United Kingdom Defence Programme: The Way Forward). Originally, up to eight of these ships would have been in a standby squadron but it was subsequently decided that all the ships should be in the running Fleet. The policy has subsequently been confirmed in answers to Parliamentary Questions, in Statements on the Defence Estimates, including SDE 88, and in response to the recent Defence Committee report on the size and role of the surface fleet (Cm 443, Government Response to the Sixth Report from the Defence Committee Session 1987-88, HC 309).

The Tasks of the Fleet and Operational Analysis

5. Judgment of the number of destroyers and frigates required is determined by two factors:

- a. the military tasks to be undertaken;
- b. analysis of the best means of undertaking those tasks, taking account of balance of investment considerations.

6. We plan to contribute simultaneously to three maritime campaigns:

- a. the Norwegian Sea;
- b. the Atlantic Sea Lines of Communication;
- c. the Shallow Sea.

7. The military tasks, which are, of course, inter-related and overlapping are:

- a. to deploy and protect ships and submarines, particularly SSBMs, from the Clyde;
- b. to conduct surveillance and intelligence-gathering;
- c. to conduct forward maritime operations in the Norwegian, Barents and Arctic seas;
- d. to support reinforcement of NATO's Northern Flank;
- e. to provide ASW support to US carrier battle groups in the Norwegian Sea and the Atlantic;
- f. to conduct ASW area operations in the Greenland-Iceland-UK gap;
- g. to conduct shallow water ASW and mine-warfare operations around the UK;
- h. to defend reinforcement and re-supply shipping for the UK and mainland Europe.

8. The MOD has conducted a number of operational analysis studies bearing on the most cost-effective way of undertaking these tasks. It is in the nature of such studies that they

cannot give precise and unequivocal numerical answers, not least because they cannot address the full complexity of modern warfare, nor the full range of scenarios which Soviet capability makes possible; but they do shed quantitative light, or insights, on the factors involved as a contribution to soundly based decision-taking. Annex A describes the most relevant work and the insights which emerged. These insights do not point decisively to any particular force mix or size, but they suggest some basic conclusions, which are consistent with the politico-military decisions taken by the Government in 1981-82 (Cmds 8288 and 8758) and the present military judgment of the Chiefs of Staff. They can be summarised as follows:

a. With the presently planned level of maritime assets, including a force of about 50 DC/FF, the UK would have a moderate capability in some tasks and a marginally adequate capability in others, but would be unable to contribute simultaneously to the campaigns listed above to the extent suggested necessary by campaign analysis.

b. There is no evidence to suggest that any major shift in the balance between surface ships, submarines and MPAs would produce a more effective UK contribution, although clearly in certain scenarios the contribution of submarines is particularly important.

c. NATO's strategy of concentrating on forward defence reduces the risk to, and therefore the escort requirements for, the Atlantic Sea Lines of Communication (SLOCs) and the Shallow Seas Campaigns, but carries with it the risk of losses and subsequent difficulty of re-deployment. The alternative of providing greater direct support in the SLOCs and Shallow Seas would, however, require a force of significantly more than 50 escorts.

9. The table below shows escort requirements by task to give what OA suggests would be a marginally adequate to moderate

capability. The right hand column illustrates how available escorts planned for the mid-1990s might be deployed at the start of hostilities:

<u>Task</u>	<u>Requirement</u>	<u>Available</u>
Clyde protection/Shallow water ASW	9-10	9
Surveillance/Intelligence/Forward Operations	8-11	6
Reinforcement by UKNLAF	8-10	8
ASW support to CVBGs	7-9	9
ASW in GRIUK Gap	3-4	3
UK/Europe and Transatlantic DeSe	6-7	6
	-----	-----
	41-51	41
	-----	-----

These figures take into account planned contributions of NATO Allies and relate to available ships only. Total force levels would need to be 15 to 20 per cent higher to account for upkeep periods.

Alliance Considerations

10. The maritime Major NATO Commanders, SACLANT and CINCHAN, have consistently highlighted their shortage of destroyers and frigates as a critical conventional defence deficiency. Together they wish us to provide at least 58 escorts in the medium term. The "about 50" policy acts as a brake on their expectations.

The Need for Replacement Ships

11. In the 1981 Defence Review, as well as establishing a force level of "about 50" Destroyers/Frigates, it was decided that ships should be paid-off after a life of around 18 years rather than given an expensive mid-life modernisation. The life of some classes of frigates and destroyers has subsequently been extended

to 22 years. Without a mid-life modernisation ships then reach the limit of their useful life in terms of the capability they can offer against an evolving Soviet capability. Where ships had already been modernised or were being modernised in 1981, they have been run on for longer, and, because of delays to the Type 23 programme, other ships' lives have had to be marginally extended. Annex B shows which ships will be paid off as Type 23s are introduced. It can be seen that the next four Type 23s (09-12) would replace four ships with an average age of 26½ years. It is important to note that the reduction from over 60 escorts to about 50 is now complete and therefore a steady order rate needs to be achieved.

Availability of Resources

12. The Ministry of Defence's procurement plans are consistent with the Government's policy and can be afforded within the funds allocated to Defence in PES 88.

Conclusions and Recommendations

13. Ministry of Defence officials point out that the Ministry's plans for employment of destroyers and frigates in war are consistent with agreed defence strategy and commitments, including the decision to retain an amphibious capability to reinforce Norway, which was announced in December 1986. They believe that sufficient evidence has been presented to justify the requirement for about 50 destroyers and frigates and that the proposed order for the next batch of Type 23s is consistent with this requirement. They further point out that, even were Ministers to require further work on the requirement aspects, this would not be a reason to defer invitations to tender for the next competition, which do not commit us to order all four ships planned, nor indeed to postpone orders, since the long term destroyer/frigate force level is not dependent on the number of ships ordered in any single batch.

OPERATIONAL ANALYSIS RELEVANT TO DESTROYER/FRIGATE REQUIREMENTS

1. The following studies, commissioned by the Defence Staff, contain relevant material:

a. DOAE's "Maritime Campaign Analysis of Three 1995 Scenarios", January 1987. The primary purpose of this study was to validate an analysis technique. It examined two North Atlantic scenarios, together with a Falklands scenario. It looked at alternative NATO operational concepts and force structures and reported on the degree of success in achieving five NATO campaign aims.

b. DOAE's "Maritime Campaign Analysis of Maritime Baseline Capability in 1998", October 1987. This study used North Atlantic scenarios which were derived from those used at sub-paragraph a above. The study looked more specifically at the effectiveness of the contribution by planned UK forces in 1998 to the achievement of NATO campaign aims. Variations were examined in Soviet forces, in NATO forces and in the assumed effectiveness of weapons and sensors.

c. ARE's "Two Tier Escort Fleet" Study, December 1987. This study examined whether, within a given total cost, RN escort numbers could usefully be increased by building an additional "lower tier" of less capable ships suited to specialised tasks. To do this it studied all RN escort tasks and assessed numbers needed for each after allowing for the presence of other NATO escorts where relevant.

d. DOAE's "Maritime Campaign Analysis of UK Force Mixes in 2008", July 1988. This study examined the capabilities of possible UK force mixes to undertake expected tasks within the NATO environment in the year 2008. Many trade-offs of different UK forces were examined as well as alternative

force deployments and varying weapon and sensor performance assumptions.

2. These studies produced the following insights relevant to a consideration of frigate numbers:

a. 1995 DOAE Study

(1) 'Air defence need not be solely a matter of fighters. Two Type 42 destroyers assumed to be deployed with UKNLAF make a useful contribution to the group's survival'

(2) 'Except against fourth generation nuclear submarines, NATO systems planned for 1995 appear to provide a robust capability for deep field ASW operations in those areas where air and surface assets can be deployed - perhaps to the extent that diversion of assets to direct support tasks could be considered.'

b. 1998 DOAE Study

(1) 'An indirect contribution to the air defence of the amphibious forces is made by using UK ASW resources in support of US carriers. Such support prolongs carrier survival and preserves their AAW capability.'

(2) 'Towed array frigates make a significant contribution to the attrition of submarines that threaten US CVBGs. Absence of UK FFTA leads to much greater reliance being placed on the carriers' close-in ASW defences. Loss of the ASW deep field has major implications for the overall ASW battle and the achievement of NATO campaign aims, particularly as CVBGs are not the only units that require protection against submarine attack.'

(3) 'UK ASW forces make their greatest contribution when the US carriers have not reached the Norwegian Sea by H-hour. Operations by UK towed array frigates, MPA and COMASWSTRIKFOR make substantial contributions in the Norwegian Sea'

c. ARE Study

(1) 'Unless it is to have only marginal survivability and flexibility the UKNLAF needs at least 7 to 9 close escorts, preferably 10-11. If the force is escorted by a CVS ... escort requirements are in principle reduced somewhat, but in practice the need could be felt at some point to detach the CVS for other purposes. Such a group would require 8-9 close escorts ... in addition to those associated with the UKNLAF itself.'

(2) 'Eight to nine close escorts should allow FOF3 to undertake most missions [in support of the Strike Fleet] with a fair prospect of CVS survival, although in the most demanding cases postulated up to 16 could be required. To allow for possible escort losses prior to the arrival of the CVBGs a further 3-4 escorts ... are required.'

(3) 'A minimum ability to mount patrols across the ocean fronts which might be the favoured deployment routes of Soviet submarines from the Kola could be provided by 6 to 9 distant escorts. A force of 12 to 15 would provide a good level of overall coverage with a margin for attrition, while 16 to 20 distant escorts would meet nearly all forward surveillance needs'

(4) 'In the GRIUK Gaps a force of 3-4 distant escorts is the minimum useful level; a reasonable barrier could be maintained with 6 to 8. Shallow water ASW operations in the Northern North Sea, NW Approaches and

SW Approaches/English Channel areas require a minimum of 3 groups, each of 3-4 ships with good hull-mounted sonar and land-on EH101 facilities. A fourth group or the use of land-based helicopters would provide flexibility to reinforce areas as required. SSBN protection will be provided by units in the NW and SW Approaches; if additional units dedicated to this task are thought appropriate, 1-2 ships should be enough.'

(5) 'The expected threat of 4 to 8 submarines [to transatlantic reinforcement and resupply shipping] does not justify the large-scale deployment of defensive assets needed to form and protect convoys. If a concept of independent sailing, with switching between 2 separated shipping lanes, to force submarines to redeploy through ASW assets, were adopted, then 4-5 distant escorts with EH101, supplemented by RPA, might be sufficient. However, in the face of a maximum threat of 15 to 30 submarines the level of potential losses would demand some form of direct support. If convoys were formed a minimum escort of 3-4 ships would be required, although this would not really be adequate against submarines standing off at 40km and using wake-homing torpedoes: 5 to 7 escorts would be necessary under these circumstances. Nine such groups of escorts would be required.'

(6) 'The likely low level of submarine and air threat in the Southern North Sea suggests that 1-2 escorts should be sufficient to support sailings from UK to the Channel ports. Shipping to BALTAP could require an escort group of 3-4 ships. Of the total of 4-5 ships, at least 2 should be SDMS-fitted.'

(7) 'The Netherlands, Germany and Belgium would contribute 19-20 DD/FF to the tasks discussed above.'

French and Danish escorts might also be available but the actual level of support likely to be forthcoming is very uncertain.'

(8) 'With a build of 55 to 65 escorts the RN can have a moderate capability in some areas and a marginal one in others.'

d. 2008 DOAE Study

(1) 'A force mix of escorts with the flexibility to bias their AAW or ASW capability as the situation dictates would be highly advantageous'

(2) 'The extra MPA force mix achieved at the expense of some FCCBs and SSNs leads to no significant change in overall ASW capability'

(3) 'Shallow water ASW would still best be conducted by ships, MPA and helicopters using active search systems.'

(4) 'Effective ASW operations demand an all arms approach with ships, submarines and aircraft all having a contribution to make.'

(5) 'NATO submarines made the major contribution to NATO ASW and accounted for over half the attrition of surface targets that operated under a substantial air defence umbrella. More generally, as NATO submarines were the main threat to these groups anything that degraded Soviet ASW capability was beneficial'

SECRET

ANNEX B

Financial Year	Ships new to service	Ships to be paid off	Age on Pay-off (Years)	Force Level as at 31 March
1989				47
89/90	Type 23-01 Type 22-14	Nov 89 Jan 90	HMS ACHILLES Jan 90	19 48
90/1	Type 23-02 Type 23-04	Nov 90 Mar 91	HMS CLEOPATRA Mar 91	25 49
91/2	Type 23-05	Oct 91	HMS BRISTOL May 91	18 49
92/3	Type 23-06 Type 23-07	Jul 92 Feb 93	HMS ALAZNE Jun 92 HMS PELOLOPE Jun 92 HMS MINERVA Nov 92 HMS DANAE Mar 93	19 28 26 25 47
93/4	Type 23-08 Type 23-09	Jul 93 Dec 93	HMS AMAZON Jun 93 HMS PBOEBE Feb 94	19 28 47
94/5	Type 23-10 Type 23-11 Type 23-12	Jun 94 Dec 94 Mar 95	HMS CHARYBDIS Apr 94 HMS ANDROMEDA Jul 94 HMS SIRIUS Oct 94	25 25 28 47
95/6	Type 23-13 Type 23-14 Type 23-15	Jun 95 Sep 95 Dec 95	HMS AMBUSCADE Apr 95 HMS JUPITER Sep 95 HMS HERMIONE Mar 96	20 26 27 47
96/7	Type 23-16 Type 23-17 Type 23-18	Apr 96 Sep 96 Feb 97	HMS JUNO Apr 96 HMS ARGONAUT May 96 HMS SCYLLA Mar 97	28 29 27 47
97/8	Type 23-19 Type 23-20	Sep 97 Jan 98	HMS ALACRITY May 97 HMS ACTIVE Jul 97	20 20 47
98/9	Type 23-21 Type 23-22 Type 23-23	Jul 98 Oct 98 Mar 99	HMS AVENGER May 98 HMS BIRMINGHAM Nov 98	20 22 48

Harland and Wolff

3.31 pm

The Secretary of State for Northern Ireland (Mr. Tom King): With permission, Mr Speaker, I wish to make a statement about Harland and Wolff. We announced in May 1988 that we were prepared to consider approaches from those interested in acquiring the yard. Since then a number of possibilities have been pursued. These have recently been narrowed down to two serious contenders, BT Shipping and a management-employee buy-out team led by Mr. John Parker, the current chairman of Harland and Wolff, and supported by Mr. Fred Olsen through two of his leading companies.

I can now advise the House that, having considered the proposals made by these two contenders, I have today approved, on behalf of the Government, heads of agreement for the sale of Harland and Wolff plc to Mr. Parker and his MEBO team, backed by Mr. Olsen.

The management-employee team and the Olsen companies will subscribe for £15 million of share capital to a new company. The company will then acquire the assets and the business undertaking of Harland and Wolff for approximately £6 million, net book value. The Government will advance to the new company £60 million of loan stock, on a repayment basis linked to performance.

Terms have been agreed under which the new owners will complete the single-well oil production system vessel for BP and the auxiliary oiler replenishment vessel for the Ministry of Defence. The Government will provide grant assistance of £38.75 million towards the cost of rationalising the activities of the yard—including new capital expenditure.

Under this agreement, Olsen companies will order three Suezmax tankers of about 150,000 tonnes each. I have agreed to offer intervention aid on them within the limits permitted by the European Community. The initial orders will provide work for the yard until the end of 1992.

The new company will therefore receive from the Government repayable loan stock and grant towards rationalisation of £98.75 million and intervention aid on new merchant orders.

Furthermore, to enable the company to raise performance guarantees necessary for the financing of its operations in its early years, the Olsen companies have agreed to make a recourse commitment for use by the new company to support predelivery ship financing. The Government will match this.

The existing liabilities will remain with the old company and the Government undertakings in respect of these liabilities of Harland and Wolff will not extend to the new company.

Beyond the terms of the heads of agreement, the Government will not provide any other special support to the new company except intervention aid and other grants normally available to other private sector companies in Northern Ireland. In this respect, I plan to repeal my powers in relation to the yard in public ownership contained in the Aircraft and Shipbuilding Industries (Northern Ireland) Order 1979.

The terms of the agreement are subject to contract and also a number of conditions including the approval of the European Commission, with which initial discussions have been held, and also the agreement of the Norwegian authorities. Critically also, it depends on achieving the

support of Harland and Wolff employees. In particular, they will be invited to invest in the new company. To this end, a prospectus will be issued by the new company in the summer. Completion is planned for early September.

In respect of funding, provision was set aside in the Northern Ireland block for support to Harland and Wolff under present arrangements, and I hope to be able to cover the costs of disposal from within the block without any disruption of other Northern Ireland programmes.

I am pleased to make this announcement today which offers the hope of a much brighter future for Harland and Wolff. This famous yard has experienced a steady decline in employment over many years, and the chances of its survival were bleak. This proposed transfer to the private sector under a management and employee buy-out led by the present chairman, Mr. John Parker, and reinforced by the strength and well-established reputation of Mr. Fred Olsen and his companies, offers the chance of a new beginning and comes at a time when there are signs of an improvement in the shipbuilding market.

A lot of us have worked hard to try and make it possible for Harland and Wolff to have this new chance—none more so than Mr. John Parker, who deserves great credit for his unstinting efforts. The challenge now is whether he will get the support to bring it to reality. This is not the end of the challenge. This is just the beginning for all those in Harland and Wolff to show that they can succeed again in the tough and competitive world of shipbuilding. I believe that the management and employees at Harland and Wolff, together with Mr. Olsen and his colleagues, are ready to meet that challenge and we wish them well.

Mr. Jim Marshall (Leicester, South): First of all, I thank the Secretary of State for making his announcement before Easter and at last putting an end to all the speculation about the future of Harland and Wolff. We all welcome the end of the uncertainty. However, it will come as no surprise to the Secretary of State that we believe that the Government's whole approach to the privatisation of Harland and Wolff has been handled in a particularly clumsy and insensitive manner, which has directly contributed to the low level of morale among the work force and to the loss of highly skilled staff, not just from Harland and Wolff, but from the economy of Northern Ireland as a whole.

Additionally, we feel that the decision that the Government made in the middle of last year to withhold intervention funding and their refusal to permit the existing company to tender for new orders seriously undermine the existing company's position and will make it that much more difficult for the new company to succeed.

Nevertheless, we recognise that, once the Government had made the decision to privatise—I repeat that my party deplors that decision and that we still continue to oppose that policy—they had a difficult choice to make between the rival bids. However, the Secretary of State will recall that, in our debate a few days ago, I made it clear that the official Opposition preferred, and always have preferred, a management-employee buy-out as we believe that it offers the prospect of greater security for the future of the company, especially in the longer term.

I should like to ask the Secretary of State some specific questions. He referred to preliminary discussions with the European Community. In those discussions, did he receive



10 DOWNING STREET
LONDON SW1A 2AA

From the Private Secretary

21 March 1989

HARLAND AND WOLFF plc: PRIVATISATION

The Prime Minister was grateful for your Secretary of State's minute of 20 March. She was pleased to note the progress made and is fully content with the proposed agreement with the management/employee team and the Fred Olsen companies.

I am copying this letter to Carys Evans (Chief Secretary's Office).

PAUL GRAY

Stephen Leach, Esq.,
Northern Ireland Office

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PRIME MINISTER

HARLAND AND WOLFF PRIVATISATION

I mentioned to you at the weekend the possibility of a successful outcome to the negotiations to privatise Harland and Wolff.

Tom King's minute of this evening (attached) confirms this, and seeks your agreement to the proposed terms of a sale to the MEBO/Fred Olsen consortium. The terms are not ideal, with in particular some degree of open commitment on SWOPS. But in all the circumstances it is an extremely good outcome:

- a net cost of £231 million within the cost of closure;
- preservation of the majority of the existing jobs;
- costs being contained within the existing provision in the Northern Ireland block, subject to a possible small bid on the Reserve in 1990-91.

Although John Major has not seen the precise terms of Tom King's minute, the Treasury has been closely involved both in the negotiations themselves and the drafting of the document, and John Major has signed up to the key elements of the deal. George Guise has also been briefed in detail on the proposals, and is content with them.

Content to agree the proposed privatisation terms?

Derek King

(PAUL GRAY)

Duty Clerk.

7 as mt

20 March 1989



Prime Minister

Harland & Wolff PLC: Privatisation

I now seek your agreement to terms for disposing of H&W, reached after lengthy negotiations throughout last week with the potential purchasers - a management/employee team joined by the Fred Olsen Companies. John Major has agreed to the terms.

The objectives we sought in these negotiations were, first, to achieve sale within the cost of closure; second, to remove any long-term liability and to keep to a minimum any responsibility for existing liabilities; and third, to establish a privatised company on a basis which provided reasonable prospects of viability. If the third objective in particular can be achieved, then the contribution of an independent, successful yard to the Northern Ireland economy, and morale, will be enormous. The terms on which Fred Olsen has agreed to become involved show that he is a serious investor and they will enable us to save initially 2,500 of the 3,000 jobs at the yard. I therefore believe disposal of H&W on these terms to be a very great prize.

The terms for disposal reached with MEBO/Olsen are described in the attached annex. H&W will hive down its assets to a new company, the share capital of which will be sold for a sum of £6m to a company to be formed by MEBO/Olsen (H&W 89). The debts of the old company will remain with H&W. In sum the deal has a net cost to us of £231m and the notes to the annex explain the headings under which this amount



will be disbursed. The structure is intended to offer the best defence to the European Commission, to whom the terms will have to be notified; and to offer the management the greatest incentive to minimise costs on existing contracts. I have also arranged to take a share of any profits on property transactions so that the new owners do not unduly benefit from this secondary activity; such profits will also expedite loan repayments.

The negotiations raised two particularly difficult points: first the handling of liabilities on the two existing contracts (SWOPS for BP; and AOR for MOD); and second the transfer of tax losses. On the contracts - for which Government is ultimately responsible - both will be subcontracted to the new company. In respect of AOR we have secured that, in return for our covering the present estimated further costs plus an incentive fee, the MEBO will accept all risk with no recourse to us if costs escalate beyond present estimates, so that we have a clean break. On SWOPS, while I have not been able to get a completely clean break, I have ensured that the MEBO would bear equally with Government the cash cost of all cost escalation. H&W 89 will bear the first £2.7m of any cost overrun, with the Government and H&W 89 sharing the next £12.3m equally. If extra costs escalate beyond this level, the Government will carry the immediate cash costs, but 50% of these will be advanced as subordinated loan stock and will add to the company's repayment obligation. The effects of this will be to reduce the cash flow impact on the company in its early years but to maintain financial discipline on it.

I am disappointed that it has not proved possible to remove all liability for the company immediately, but I am clear that the price of this would have put the viability of the new company in severe jeopardy. On the other hand, we have put on the company what I judge to be the right mixture of incentive and responsibility to

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promote the efficient completion of SWOPS. I hope you can agree to this arrangement.

The second focus was tax losses. H&W currently have tax losses in excess of £400m. MEBO/Olsen originally sought transfer of £200m. After lengthy negotiation in which tax consultants and Inland Revenue participated, I now intend to offer about £60m for transfer although they are still seeking £75m. I have insisted that the use of these tax losses be confined to the existing core businesses within Northern Ireland.

I have agreed with John that I will endeavour to bear all the costs of disposal within the Northern Ireland Block, although I could not at this stage entirely rule out a small bid (up to £11m) on the Reserves in 1990/91. He has agreed to consider sympathetically any case which I might find it necessary to mount to cover additional costs in the event of an overrun on SWOPS.

I believe that these overall terms represent the best deal achievable for the taxpayer which provides a basis for viability of the new company. They also represent, in my judgement, the clearest achievable break with our liabilities towards the yard, and I plan to repeal my powers in relation to the yard in public ownership contained in the Aircraft and Shipbuilding Industries (NI) Order 1979. I also take real encouragement from the involvement of Fred Olsen in terms of financial control, management resources and equity risk. I suggest therefore that the present terms offer an opportunity to break with the past and at last to get private sector disciplines and responsibilities into an undertaking that has suffered for far too long from the damage of state dependence. I strongly recommend them to you.

S. Spenser.

20 March 1989

pp TK
(Approved by the Secretary of State and signed in
CONFIDENTIAL his absence)
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Terms for Proposed Acquisition of H&W by MEBO/Olsen

Disposal of Assets

1. H&W will hive down its assets to a new company, the share capital of which will be sold for a sum of £6m to a company to be formed by MEBO/Olsen (H&W 89). The assets will include fixed assets, stock and other current assets, and leasehold land and property. The stock will exclude any items related to SWOPS or the AOR. The terms under which the leases will be transferred will be subjected to negotiation with the leaseholder (Belfast Harbour Commissioners) but DED will receive 25% of any profits resulting from the redevelopment of any land or buildings in each of the first 5 years trading; the percentage share to decrease to zero in equal stages over the next five years. Should profits exceed £10m in any one year DED's percentage share will double on the excess.

2. Conditions to the sale are:-

- a. MEBO/Olsen to demonstrate to the complete satisfaction of DED that it has the financial resources needed to complete the transaction; the proposal is that H&W 89 will raise up to £15m share capital, with the Fred Olsen companies providing up to £12m of that sum;
- b. The Fred Olsen companies to demonstrate that they have the resources to meet their share of the obligations under the proposed sale agreement;
- c. The Fred Olsen companies to place contracts for three Suezmax type vessels - and arrange satisfactory financing;

- d. Beyond the terms of this offer, DED not to provide any cash, guarantees or financial support for H&W 89, except intervention aid on terms and conditions applicable at the time of application and other grants normally available for approved expenditure.

3. Most tax losses will be extinguished but about £60m of tax losses will be offered to H&W 89 although they have sought £75m. This is to provide shelter for the taxable elements of the package of assistance and for profits needed to repay the subordinated loan stock (paragraph 4f). Expert advice on the extent of the shelter required and the means by which it can be provided is being prepared by tax advisers representing MEBO/Olsen, DED and Inland Revenue. The use of the losses will be restricted to H&W 89's core businesses in Northern Ireland.

Government Assistance

4. a. Intervention Aid Intervention aid at the rate of 26% of the estimated cost of building the three vessels to be ordered by the Fred Olsen companies; not more than £37m. H&W 89 will be able to retain any profit made on the construction of these vessels.
- b. Recourse Facility A sum of £33.5m will be paid into an escrow account to be administered by DED and DED will ensure that, with interest accrued, the total in the account reaches £39m by the end of year 3. Any further interest will be paid to DED. The amount in the account will be available to meet not more than one half of any audited claim against H&W 89 under counter indemnities given to third parties as security for predelivery finance. The Fred Olsen companies (or other guarantor) will bear the other half of any claim. A claim can be

made only where the consequences for H&W 89 of meeting the claim itself would be cessation of trading. Any unused balance of the facility will be repayable to DED at the end of year 8 (or earlier if the company is in receivership or liquidation). The company may, however, ask DED to terminate the facility earlier. If full repayment is made at the end of year 3, an incentive payment of £12m will be made to H&W 89 out of the facility, this incentive to reduce proportionately for full repayment in a later year to zero in year 8.

- c. Investment Programme Grants of not more than £28.75m at rates of 40% or 100% on expenditure of £32.9m to restructure the yard and improve its efficiency, to be completed by 31 March 1992.
- d. Redundancy Costs DED to meet the cost of redundancies to be implemented before completion to reduce the workforce to the level required by H&W 89 (costs not included in the attached summary). On completion, H&W 89 will seek to terminate the existing supplementary redundancy scheme and DED will make a payment of £10m towards the cost of buying out the scheme and/or towards redundancies after completion.
- e. Pension Scheme This will be actuarially reviewed at completion. Any surplus up to £2m will be left in place but any in excess of £2m will be repaid to DED.
- f. Subordinated Loan Stock DED will subscribe £60m of unsecured loan stock on the following terms:
 - i. as regards repayment; once cumulative earnings available for distribution (whether distributed or

not but excluding grants received from DED) have exceeded 130% of the original share capital, then repayments should be made up to three-quarters of distributable earnings in any subsequent year. These sums may, however, be retained in which case they will rank for interest at 15%. H&W 89 may repay in full or in part at any time and the ultimate repayment date is 2009 for interest bearing stock and 2019 otherwise.

- ii as regards interest; 15% on outstanding repayments only.

Existing Liabilities of H&W

- 5. a. Existing Orders H&W estimate of the net costs to complete SWOPS and AOR are £6.1m in the period to 31 August 1989 and £9.9m thereafter. DED will offer H&W 89 £35.35m (which sum takes account of underutilized capacity during construction of AOR) to complete these orders on its behalf after 1 September. This offer will be made on the basis that H&W will take full responsibility for completion of AOR. As regards SWOPS, H&W 89 will bear the first £2.7m of any cost overrun above the present estimate, DED and H&W 89 will share the next £12.3 m equally (not included in the summary), and DED will bear any cost overrun beyond £15m. However, half of any DED payments beyond a cost overrun of £15m will be advanced as subordinated loan stock and will be subject to its terms (para 4(f)). Furthermore, the £60m loan stock referred to in para 4(f) will be advanced on a staged basis only against achievement of milestones for the completion of SWOPS.

- b. Other Liabilities H&W will retain all rights and liabilities arising out of past contracts including any rights of recovery against MOD on the ATS contract and ship financing obligations.

SUMMARY OF PAYMENTS

	£m	£m
Net costs of completing existing orders (paragraph 5(a))	41.45	
Historic ship financing costs and other existing liabilities (paragraph 5(b))	26.3	
Compensation for ending enhanced redundancy scheme (paragraph 4(d))	10.0	
Investment Programme (paragraph 4(c))	28.75	
<u>less</u> Purchase of Assets (paragraph 1)	<u>(6.0)</u>	100.5
Subordinated loan stock (paragraph 4(f))		60.0
Intervention Aid (paragraph 4(a))		<u>37.0</u>
		197.5
Recourse Reserve (paragraph 4(d))		33.5

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PRIME MINISTER ²

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HARLAND AND WOLFF

There was some speculation in the press today that the talks on a possible 'sale' of Harland and Wolff to the management buyout/Olsen team were proceeding well.

I have checked the position with Tom King's office, and there is some substance in the stories. NIO are hopeful of reaching agreement, broadly in line with the policy of keeping costs within the costs of closure, and a formal report may be coming to you early next week. If all goes well, Tom King would like to be able to make a statement before Easter. If that can be achieved it would be very good news.

Navallos.

Meantime, the discussions on the sale of Shorts proceed, with the two interested parties of Bombardier and GEC/Fokker. The timetable here is slightly slower, with both companies having until the end of April to come forward with their detailed proposals.

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Plcb.

PAUL GRAY
17 March 1989

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PRIME MINISTER

1 March 1989

NORTHERN IRELAND INDUSTRY

The main subject is Shorts where Tom King's paper proposes dealing exclusively with one potential purchaser throughout March. Prospective suitors for the other two businesses, Harland and Mackies, continue to appear and disappear although the joint Olsen/MEBO proposal for Harland is the most positive yet.

HARLAND AND WOLFF

The Olsen initiative should be encouraged under the absolute constraint that the Government's financial outcome must under no circumstances be worse than closure. A total cost limit of £275 million should therefore be set at E(A). This figure already appears to be heavily padded with contingencies and maximum estimates included at every stage of the calculation. Nevertheless, in order to achieve a settlement, it makes a realistic working limit. Fred Olsen has a respected reputation and has put his name to a serious letter of intent. This is far more encouraging than last year's 'make believe' proposals from Ravi Tikoo.

It is nevertheless important to make the cautionary point that to 'be seen to explore all the privatisation possibilities' must not be interpreted as a licence to keep Harlands bleeding for evermore on the back of the tax payer. If the Olsen/MEBO deal disappears then the yard must be closed. Whatever the short-term popularity consequences, it can do no good to the Province or to the Government to let this drift on much longer. Harlands is one of the highest cost and most incompetently run shipyards in the

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world. The hard prospect of closure may incline the workforce to reduce activity to a crawl but this could be counteracted by incentive payments linked to deadlines. Such additional costs would be part of the overall closure decision and should be so treated.

Hopefully we shall not get to this position but in pursuing the Olsen deal, the reality of the closure alternative must be recognised and, if necessary, quickly implemented. It is no solution to enter a vicious circle of procrastination so the yard runs out of work before a decision is made. That would leave a longer and blacker political mark than planned closure with adequate planning.

MACKIES

The suitors for Mackies change every time the subject comes up. In December we were told that the only alternative to a Howdens sale was 'complete closure of the company'. Now Lummus has reappeared but where this will lead is pure speculation. However, it would do no harm to remind the meeting that the number we were talking about for Government support for a Mackies sale was a maximum of £20 million.

Indeed, you initially suggested that might be tranced with an initial payment of say £10 million and the remainder dependent upon performance. If either the Lummus or Howden initiatives mature into a real purchase, then it would be better to let the £20 million go in one lump and be shot of Mackies. I understand that Lummus is a competent firm which should have the capability of turning Mackies around although not as strong as Howdens.

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It might be appropriate to remind Tom King of his own words on Mackies - 'I am determined that the situation will not be allowed to drift'.

SHORTS

I have seen the various proposals for purchasing Shorts. Only that from Bombardier reads like a coherent strategic plan - see Annex A. Even that is qualitative without proper numerical analysis. The strength of the Bombardier proposal is that their own business plans make it essential to reach a decision on Shorts very soon. It is appropriate to use this to our advantage but not at the cost of ending up with no sale through sending potential purchasers away too soon.

Only the joint GEC-Fokker, and possibly the MBB proposal, seem worth pursuing with any urgency. It is improbable that either of these could be finalised by the end of March, although it could be possible to push Fokker within a two month deadline. I have suggested that Kleinworts tell Fokker that they have a potential rival capable of completion by the end of March. If Fokker could make the same commitment, they could examine the company simultaneously. This might be administratively awkward but one possibility might be to allow both suitors more time. I understand that Tom King is also now moving in this direction. No individual purchaser would be seen to be on some 'inside track' and, if Bombardier fell away, it would leave at least one other active contender.

If however Bombardier is given a de facto exclusive, there must be an absolute deadline at the end of March which should not be extended to resolve detailed matters. As with

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BAe/Rover, an overall sum of say £600 million could be set as the broad framework for the detailed deal. It is difficult to be adamant about the size of this sum in advance but last week's Select Committee mentioned a figure of up to £850 million which Kleinworts have privately indicated will probably cost the government an extra £100 million! It might therefore be appropriate to start Tom King with a limit of £600 million with the requirement that he return to E(A) if he needs to go higher.

don't
reveal
you
know
this!
P.L.G.

The Government could defend itself against allegations of not achieving the best price by reaching a settlement within the figure recommended by the Select Committee and also pointing out that Bombardier was the only company that actually made an offer for the entire business. The GEC/Fokker deal separates the missile division straight away and the same sounds true of the MBB proposal (see Annex B). In any case MBB can only be tentative because of the necessity of prior resolution of a merged business strategy with Daimler-Benz. MBB therefore seems a limp fallback and very much the third contender.

The realistic alternative to Bombardier is Fokker/GEC but this would mean breaking up the company in opposition to the views of management, Northern Ireland politicians and the Select Committee. This should be a strong defence if a Bombardier deal is concluded.

CONCLUSIONS AND RECOMMENDATIONS

- 1 On Harlands, set an absolute limit to the Olsen deal of £275 million failing which closure must automatically follow.

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- 2 Take note of the new situation at Mackies reminding King of the £20 million limit.
- 3 On Shorts reiterate your insistence that the actual transfer of the £390 million is dependent on both the appointment of the Finance Director and the rearranged capital structure which effectively limits their further borrowing headroom to £10 million. (This has the same effect as reducing their borrowing limit from £400 million to £10 million because the Government funding is also a loan which itself uses up £390 million of Shorts borrowing limit leaving only £10 million left).
- 4 Propose that an exclusive be given to Bombardier only if Fokker/GEC would be unable also to reach a quick decision. Emphasise that if an exclusive is given to Bombardier, the end March deadline is absolute. 16
- 5 Support a parallel investigation by both Bombardier and Fokker (over say two months) if King offers this alternative.



GEORGE GUISE

Annex A - Extract from Bombardier's proposal.

Annex B - Extract from MBB's letter.

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Logistic Equipment Division

This division was established in 1981 to manufacture vehicles for the transportation of troops and materials. Products in this division include a 2.5 ton truck licensed from AM General, the four-wheel drive all-terrain ILTIS jeep (with technology acquired from Volkswagen), as well as the parts for these vehicles. The overall strategy in this division is to cover the full range of vehicle sizes through joint ventures and licensing agreements.

Vehicles have been delivered to the Canadian, Belgian and West German Armed Forces, and we intend to exploit these bases to further develop domestic and international markets.

6. Bombardier's plans for the future

Bombardier Inc. intends to continue its strategy of building on the strengths we have established in the transportation field, and to remain a financially strong company with good profitability.

We will continue to strengthen our standing in major markets in Europe, North America and Asia. We intend to pursue product diversification in the transportation industry, seeking a counter-cyclical mix of products for the consumer, industrial and defence markets. Expansion will be achieved through internal development, joint ventures and acquisitions.

7. Bombardier's interest in acquiring Shorts

Bombardier believes there could be an excellent strategic fit between our company and Short Brothers. There is complementarity between our three main areas of business and our principal geographical market bases. We can immediately project that both companies could benefit from the significant synergies to be gained in the areas of engineering, research and development, production, and marketing.

We see the potential, with the proper investment and private sector leadership, to set Shorts on the path of growth and profitability that would be to the mutual benefit of Bombardier, the British Government and the community of Northern Ireland.

In the context of Europe 1992, free trade between Canada and the United States, and increasing global competition in the defence and aerospace industries, the joining of strengths between two medium-sized but strong players will provide mutual advantages and open up opportunities which may otherwise not be available.

Bombardier is not a financial holding company which buys and resells assets to increase its worth. We are committed in the long-term to the transportation equipment sector including the aerospace and defence industries, and the acquisition of Shorts would be a long-term investment which would complement our current manufacturing and corporate global strategy.

8. Bombardier's assurances regarding Shorts

From our current assessment of the situation of Short Brothers, we would be prepared to consider the following commitments.

A separate entity based in Northern Ireland

Bombardier's intention would be that Short Brothers continue to operate as a separate whole entity under its present name and that it be developed with a long term perspective similar to what we have pursued with Rotax in Austria, and with B.N. in Belgium. Headquarters, as well as manufacturing and R&D facilities would remain in Northern Ireland.

Retention of Shorts Shares

It is our intention to acquire Shorts as a long-term investment and we would be prepared to give assurances that we would retain a shareholding for a minimum of three years.

May not sound long but is quite a commitment.

As part of our strategy in an increasingly complex competitive environment where projects and corresponding business risks are growing in scale, we see great potential for complementarity and specialization between Canadair and Shorts in a manner which will increase the viability and competitive advantages of both organizations.

Bombardier is committed to the aerospace sector, and we have demonstrated our capacity to stand behind our products and businesses through good and bad times. Our finances are solid and we have access to capital markets in North America and in Europe. We are prepared to make the appropriate long-term managerial and financial commitments for the future development of the company.

Future Strategy

Bombardier sees considerable advantages in maintaining Short Brothers as a complete entity, and in strengthening the individual divisions that currently exist. A decentralized structure is one of our well served management principles, and we believe that responsibility and accountability should be pushed down to where the action takes place. We encourage our managers to look for new business opportunities and to seek innovative solutions to problems. We strive to recognize, support and reward such initiatives.

Our experience with the privatisation of Canadair has further proven the benefits of our management philosophy. Since its acquisition by Bombardier, Canadair has achieved profitability after a long history of significant losses. This profitability was achieved in the first two years of our ownership. Since then, we have made significant investments to expand its technological base, upgrade product lines and develop new markets, including a CS 15 M study on opportunities in the regional aircraft market.

Used much Canadian govt money but it did make it profitable.

It would be our intention to pursue a similar strategy for Short Brothers. Based on the information at hand, we have identified clear preliminary strategies for each of the three main divisions of the company.

Aircraft

We see good market potential for Shorts' total systems capabilities in the aircraft sector in the long term. We also feel that Shorts' technology and the experience gained in the SD3 series, the Tucano and the Sherpa could be supported and further exploited. The commitment to product support for Shorts aircraft would also be continued.

In the past months Bombardier has invested considerable time and effort in order to become familiar with Short Brothers. In particular, advanced discussions between senior managements have been held to explore potential areas of collaboration and synergies on the Regional Jet project.

In the short term, we believe we should go ahead with our Regional Jet which we have developed based on proven Challenger technology. In spite of some advantages which could be provided by Shorts' proposed FJX, our Regional Jet project will minimize the technical and financial risks, and will allow a timelier response to immediate market demand. In doing this, we could directly share the program with Shorts and utilize its capabilities by engaging its personnel in specific engineering, tooling and manufacturing requirements.

We would also intend to have Shorts share in the responsibility for the development of a second generation commuter jet.

As part of our strategy, Bombardier anticipates good potential synergies between Shorts' and our own military aircraft in the North American and European markets. In particular we foresee significant opportunities in the further development of the Tucano trainer for the Canadian Armed Forces and other markets.

Aerostructures

Given the current state and evolution of the aircraft industry, the aerostructures market clearly has great potential for future growth. Short Brothers and Canadair are recognized for their expertise in the design and production of aerostructures and we see promising avenues for complementarity and synergy in this area. It should be noted that both Canadair and Shorts have major subcontracting arrangements with Boeing.

For instance, the mandate for composites manufacturing and technology development in our aerospace sector could be given to Short Brothers for its Queens Island and Dunmurry sites.

Furthermore, Canadair and Short Brothers should share costs and market information in order to strengthen the profitability of each organization.

Missiles

Shorts has demonstrated its ability to excel in the development of state of the art missile systems. It would be Bombardier's intention to support the company's strategy for continued growth in these markets through internal development and joint ventures. Furthermore the Canadian Armed Forces has recognized a need for the type of missile developed by Shorts.

We also believe there is considerable potential for an integrated approach to the European and North American missiles and surveillance markets. We would intend to pursue significant expansion of this business through alliances with other European and American partners.

In order to capitalize on defence procurement opportunities, with the collaboration of the Canadian and British Governments, Bombardier would consider a joint venture on the technology and development of our surveillance systems with Shorts. This could be done in conjunction with a review of the requirements of HM Ministry of Defence.

Employment levels

Bombardier recognizes the impact of Shorts on Northern Ireland's economy. As outlined in our mission statement, Bombardier is committed to ensuring our employees quality of life, job security and training. As previously mentioned, since Canadair was acquired from the Canadian government, approximately 700 new jobs have been created.

Within the framework of the objectives we have expressed for Short Brothers, Bombardier would do everything in its power to enhance employment opportunities in Northern Ireland and the current growth in commercial aircraft orders should help this.

As previously mentioned, the Regional Jet project could have a significant impact on employment opportunities in the near future through the creation of approximately 500-600 jobs which should endure over 10 years for Shorts employees, plus the additional work provided in composites manufacturing. We can also foresee new employment opportunities emanating from the surveillance systems and other projects. In addition, we are prepared to collaborate with HM Government's employment objectives for Northern Ireland, and will work with the Government in meeting these objectives.

We also recognize the importance of economic spin-offs and indirect employment provided by Short Brothers in Northern Ireland, and would strive to maintain and improve them where possible.

Existing Obligations

Bombardier's intention would be to continue to respect the commitments of Short Brothers towards its customers, subject to a review of these obligations.

? This may be a hint of wanting
HMG to continue some of the
present assurances

Further Assurances

Bombardier would consider making the following other commitments to ensure the future success of Short Brothers in Northern Ireland:

- It is our intention to continue working with present management

- We believe in fostering the entrepreneurial spirit of our people. In this perspective, we would explore with Shorts management ways which would allow them to participate in equity ownership.
- The Board of Directors of Short Brothers would retain substantial representation from Northern Ireland and the United Kingdom.

9. Bombardier's interest in the proposed FJX Program

The senior management of Bombardier and Short Brothers have been involved in extensive discussions regarding collaboration on the FJX and RJ Aircraft Programs. As mentioned previously, after careful review, Bombardier feels its Regional Jet project presents the best opportunity for a timely market penetration with a limited investment and acceptable level of risk.

It would be our intention however to have Shorts share in the R.J. program by involving its engineers in the design and development work, and in the development of a second generation regional jet, thus helping to maintain integrated capability in the aircraft sector.

For the immediate future, Bombardier would consider the following as a practical means of ensuring a high level of activity for Shorts Aircraft division:

- Transferring to Shorts a substantial amount of work on the RJ program, aiming for a level equivalent to that which would have been generated by the FJX. This includes approximately the 500-600 jobs mentioned previously within which is included a significant engineering task. This is based on a program of 400 RJ aircraft sold, and the manufacturing of parts which are common to the RJ and to the CL-601 executive jets. (Detailed list of work which could be transferred in Appendix C).
- Transferring all composite manufacturing for the RJ to Shorts. *jobs?*
- Developing with Shorts a coordinated sales and customer support network for the commuter market.

Bombardier feels that this long term approach, designed to build on the respective strengths of both companies, is an appropriate way to attain a strong competitive position in this market segment of the commuter sector.

10. Bombardier's requirements pursuant to this proposal

Bombardier's previous experience with the privatization of Canadair has given us valuable experience in managing the issues related to such an acquisition. Following its selection for the next stage of the sale process, we will be prepared to move quickly, but would require the following:

- The opportunity to visit Short Brothers facilities with a Bombardier team in the near future
- A complete review of due diligence information directly available from the company. A comprehensive list to be provided at the next stage of the process.
- Early discussions with HM Government regarding their intentions for restructuring the balance sheet of the company and funding for its future development.
- Joint discussions between Shorts and Bombardier management of Shorts business plan and five year pro-forma demonstrating its view of the future and its intended strategy.
- An indication of the level of Government support to be provided for work which Bombardier could immediately transfer to Shorts.
- We also believe it would be useful to meet with labour representatives in order to obtain a clear understanding of their objectives.

11. Other information in support of this proposal

Bombardier has invested two years and \$15 million in the development of its Regional Jet project, but has only recently engaged in serious discussions on potential collaboration with Short Brothers. We strongly believe, as does Shorts management, in the future of the regional jet and in the potential of our two companies to jointly establish a strong foothold in this market.

Timing

Timing is of the essence if we are to maximize market penetration of this new aircraft, and Bombardier intends to announce the launch of its Regional Jet before the Spring of 1989. Given the significance of our potential collaboration with Shorts on this project and for Shorts to obtain the greatest possible benefits from the potential acquisition and its subsequent role in engineering, tooling and manufacturing of the Regional Jet, it is critical that Bombardier obtain a clear indication of HM Government's intentions with respect to the sale of the company by the end of February 1989. *now March 31*

Bombardier's original December 1988 launch date was already delayed due to the Canadian Federal Election. Institutional and government financing for the project is nearing completion and must be finalized; Shorts participation and HM Government's support would need to be finalized beforehand. Furthermore, our negotiated quotes from suppliers expire at the end of March and would need to be re-negotiated after that time. Shorts role in the project could have a significant impact on the nature and volume of external supplier contracts.

The Board of Directors of Bombardier will meet in March 1989 to approve the launch of the Regional Jet Project. If no clear indication of HM Government's intentions is received by this time, this employment opportunity for Short Brothers will pass.

We must turn this pressure back on them by a March 21 deadline for a decision.

In conclusion, we would like to reiterate our sincere interest in Shorts and in the important synergies and strategic advantages for both companies, as well as the significant employment opportunities which could be created by allowing Canadair and Short Brothers to collaborate together under the leadership of Bombardier.

Yours sincerely,

RE Brown

Sir

Laurent Beaudoin
Chairman of the Board
Bombardier Inc.

is the leading German aerospace and defence contractor. It is involved in many prestigious European aerospace and defence programmes. Within MBB's aerospace division there are a number of developments, processes and products which are complementary to those of Shorts. Both MBB and Shorts have an established history of successful co-operation. This would augur well for the development of the two businesses following the acquisition in the context of the evolving European aerospace industry. MBB is hopeful that the acquisition of Shorts by MBB would generate substantial benefits for both businesses.

Outline plans have recently been made public for a series of transactions involving a substantial increase in the share capital of MBB following which MBB will form the major part of a new aerospace division of the Daimler-Benz Group ("Daimler"). After this proposed re-organisation, the new aerospace division will rank as one of the largest in Europe.

In light of its strong financial position, MBB has the capacity to acquire Shorts and support its development. This will be reinforced following the subscription of new capital in MBB by Daimler.

MBB is sensitive to Short's position as a significant supplier to the UK MoD. Based on the limited information about Shorts currently available it is not clear to MBB that 100% ownership of all the operations of Shorts would necessarily be most advantageous for MBB or Shorts. Additionally, 100% ownership by MBB of Shorts's missile division may not result in the most beneficial relationship with MBB's existing missile operations.

At the appropriate stage, therefore, MBB may seek approval from H.M. Government and its advisers to enter into discussions with possible partners in the acquisition of Shorts.

At this early stage it is not feasible for MBB to put forward any detailed financial proposals. However, MBB expects any proposals it may eventually make to include an offer for the shares of Shorts at a price related to the consolidated net asset value of Shorts at completion. The relevant net asset value would be a pro-forma figure reflecting the recapitalisation of Shorts and a full review of the consolidated assets and liabilities, covering, among other matters, the level of provisions, the valuation of work in progress, the off-balance sheet assets and liabilities and the financial implications of long term contracts.

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P 03385

PRIME MINISTER

HARLAND AND WOLFF PLC, JAMES MACKIE AND SONS LIMITED
AND SHORT BROTHERS PLC

E(A)(89) 4, 11 and 12

DECISIONS

1. You may wish to take the progress reports on these three companies in the following order.

12m early
30m
88m - order
Intervention

i. Harland and Wolff. The only prospect of disposal appears to be a management/employee buyout in partnership with Mr Fred Olsen. Mr King aims to follow the Govan precedent, of keeping the cost of disposal (including any liabilities retained by Government) within the cost of closure. He estimates this figure to be in the region of £275 million. The Chief Secretary is likely to press for a lower figure of £220 million. A decision is needed to enable negotiations to proceed. You may wish to ask Mr King about the prospects for achieving the disposal at either of these figures. You may wish to conclude by inviting Mr King to report progress in two months' time.

ii. Mackies. Disposal of Mackies to Howdens has been frustrated by the decision of the trustees holding Mackies shares to prefer a revised offer from the American firm of Lummus. Mr King met the trustees on Monday, and may be able to report further at the meeting. You may wish to note the position and invite Mr King to report back again in two months.

No

iii. Shorts. You may wish to invite the Sub-Committee to note with approval the decision to seek a Spring Supplementary Estimate of £390 million; and to resolve two issues. These are first, whether there should be exclusive negotiations with Bombardier until 31 March, as Mr King proposes on Kleinworts' advice; and second, whether negotiations should be conducted within a ceiling for Government support of £600 million (inclusive of the £390 million).

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MAIN ISSUES

HARLAND AND WOLFF

2. At present there appears to be only one serious bidder, the management/employee buy-out in partnership with Mr Fred Olsen. Mr King suggests that Mr Olsen's involvement makes this proposal the best opportunity yet for securing Harland's future. As a precaution, you may wish Mr Younger to confirm that there are no insuperable security implications if Mr Olsen became the part owner of a yard constructing the AOR.

Cost of closure

3. Mr King estimates the overall closure costs to be £275 million, on the basis of Touche Ross's figures: paragraph 10 and Annex B of his paper. This compares with his preliminary estimate of £240 million last July. The Treasury are sceptical for two reasons. First, the estimate has been prepared (understandably) on the basis of detailed costings from Harlands themselves. The management of Harlands have a clear interest in inflating such costings, since this will provide more headroom for their buy-out bid. Second, the estimate includes £55 million for contingencies, comprising £25 million of the £105 million cost of completing existing contracts (which is described as an estimate of the direct consequence of reduced productivity following a closure announcement) plus the £30 million contingency to take account of possible industrial unrest and disruption, wilful negligence and the risks of criminal damage. The Chief Secretary is expected to argue that this £55 million should be deducted from the estimate of £275 million for the purposes of negotiating with potential bidders: that is, that the current ceiling in negotiations should be £220 million. You will wish to consider whether the Chief Secretary's figure would be a better basis for negotiation in the circumstances.

Timetable for decisions

4. An early end to negotiations on Harlands is highly desirable. Whilst the uncertainty persists, management at the yard continues to leave. Limited progress appears to be being made with the two current orders. In December Mr King estimated that SWOPS would be delivered in June 1989 and the AOR in December 1990. His latest

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estimates are November 1989 for SWOPS and February 1991 for the AOR. You may wish to ask Mr King about his intended timetable to the conclusion of negotiations.

MACKIES

5. Negotiations on a package of Government assistance for Howdens to take over Mackies were nearly complete when the Trustees holding Mackies current shares came forward with a revised proposal from the American firm Lummus. The Trustees have accepted Lummus' offer in principle, subject to Government support being available for Lummus' business plan. Lummus had been involved at an earlier stage, but it had been understood that they were no longer interested.

6. The proposals under discussion with Howdens had involved no immediate payment for the shares but the prospect of a share in future success should that occur. The proposals from Lummus are understood to be more generous to the Mackies Trustees, who act on behalf of current and former employees of the company. Mr King met the Trustees on Monday to explain his attitude towards the Lummus proposal and to press them to resolve the future of Mackies as soon as possible. You may wish to ask Mr King to report on these latest developments and simply note the position. No immediate decisions appear to be required.

SHORTS

Capital Reconstruction

7. When E(A) met on 1 December it concluded that a once and for all capital reconstruction of Shorts would be preferable to an interim reconstruction. Mr King may therefore wish to explain briefly the reasons for deciding on a financial injection equivalent to Shorts existing debt in this financial year.

Exclusive Negotiating Rights

8. Mr King regards Bombardier's bid as the most attractive. Its proposal to buy Shorts is considerably more advanced than the others which were received. Bombardier has said that it needs to know where it stands with Shorts by the end of March, because its plans for a regional jet are far advanced and arrangements urgently need to be

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made with sub-contractors. We understand that Mr King made considerable efforts to extend his deadline when he met Bombardier's chairman on Monday, but without success. Mr King therefore proposes, on Kleinworts advice, to negotiate on an exclusive basis with Bombardier until 31 March.

9. We understand that the Chief Secretary agrees with Mr King that Bombardier's bid should be pursued. The main alternative to giving Bombardier exclusive negotiating rights would need to persuade at least one of the other bidders to pursue its bid on the same timescale. You will wish to decide whether Bombardier should be given exclusive negotiating rights until 31 March. If this period is granted and no deal is finalised, you would probably wish all remaining bids to be given time to reach the same stage of knowledge as Bombardier before any competition continued.

Ceiling for Government support

10. Mr King proposes to conduct negotiations at this stage with a ceiling of Government support of £600 million. This compares to the range of £700-850 million which the Select Committee on Trade and Industry recently suggested would be necessary, and is also below the ranges produced by Kleinworts and Touche Ross. We understand that the Chief Secretary may be prepared to allow negotiations to proceed on the basis Mr King proposes. You will wish to decide if you are also content.

11. You may wish to note that Mr King proposes that some of the Government support for Shorts could be in the form of launch aid for the development of whole or part new aircraft. He also proposes to tell bidders that there will be no objection to Shorts bidding for Ministry of Defence contracts once in the private sector. You may wish to check that the Chief Secretary, Mr Younger and Lord Young are content.

Next Steps

12. You may wish to ask Mr King to report back to E(A) in a month's time, if an exclusive period for Bombardier is agreed until 31 March. You may also wish ~~Mr King~~ to consult the Foreign Secretary and Lord Young on the handling of any further negotiations with the European Commission.

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HANDLING

13. You may wish to ask the Secretary of State for Northern Ireland to introduce the discussion on each company in turn. The Chief Secretary, Treasury will wish to respond first. The Secretary of State for Defence may wish to comment on the implications for his Department of the prospects for Harland and Shorts. The Foreign and Commonwealth Secretary and the Trade and Industry Secretary may wish to comment on the handling of discussions with the European Commission on the provision of financial support for the three companies. Other Ministers may wish to contribute to the discussion.

RJW.

R T J WILSON
Cabinet Office
1 March 1989

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ON MANPOWER: SEM'S PT 21

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PRIME MINISTER

MEETING OF E(A): 2 MARCH

There is, I fear, a daunting pile of paper for this meeting. But you do not need to read it all, and I doubt if the meeting need last too long. That means it should be over in good time by 12.30, so that you can then talk further to the Chancellor about the Budget.

I will try in this minute to summarise the issues and the bits of paper you need to refer to.

The papers are organised in two dividers below:

The first includes all those relating to Norman Fowler's proposals on Skill Centres and the Employment Service; the second, the papers on the three Northern Ireland companies - Harland and Wolff, Mackies and Shorts.

Skill Centres and Employment Service

The formal agenda has Skill Centres as the first item and the Employment Service as the second. For reasons explained below, I suggest you reverse this order.

The full list of papers enclosed is:

- Flag A - Norman Fowler's paper on the Employment Service
- Flag B - His short personal minute on the same subject
- Flag C - Minute from the Attorney General on the Employment Service
- Flag D - Cabinet Office brief on the Employment Service
- Flag E - Norman Fowler's paper on Skill Centres
- Flag F - Cabinet Office brief on Skill Centres
- Flag G - Policy Unit note on Skill Centres.

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b

When you discussed the Employment Service paper on 8 February you called for further work, particularly on the legislative implications. Norman Fowler's paper (Flag A) reports that this work is underway, and simply provides a progress report on other aspects of the proposal. In his separate minute (Flag B) he invites you simply to note the progress report and to ask him to return to the Committee in May or June when the other work is done, and the dust has settled on other issues.

But the key paper to look at on the Employment Service is the Attorney's minute (Flag C). This confirms that legislation is required:

- for the principle of privatising job centres
- and to cover various aspects of the transfer of the staff to the private sector; covering the transfer of Undertakings Protection and Employment Regulations, the redundancy provisions of the Civil Service Pension Scheme, and the Model Redundancy Agreement.

All this means the discussion of the Employment Service can be brief. You can simply note that:

- there are major legislative implications, which cannot be covered at least until the 1989/90 Session.
- Mr. Fowler will report back in May or June.
- Meantime you may want a brief discussion on some aspects of the points which are covered in Mr. Fowler's paper (see paragraphs 4-6 of the Cabinet Office brief at Flag D).

You can then move on to Skill Centres. You had a brief look over the weekend at Mr. Fowler's paper (Flag E). But I suggest all you need read now are the Cabinet Office and Policy Unit briefs at Flags F and G.

Notwithstanding his proposal to delay action on job centres, Mr. Fowler proposes to press ahead in this Session with the Skill Centres proposal, by means of amendments to the current Employment Bill. You may want to question this. The first issue to settle is how extensive is the need for legislation. It is clear that some at least of the legislative requirements for the job centres are also required for Skill Centres. That being so, would it not be better also to defer Skill Centres until the next Session?

That is the first point to settle. Having done so, however, there would in any event be advantage in having a "Second Reading" debate on other aspects of the Skill Centres proposals. I suggest you use the check list in paragraph 2 of the Cabinet Office brief (Flag F), adding in the point on page 4 of the Policy Unit brief (Flag G) about Employment and Rehabilitation Centres.

Harland and Wolff, Mackies and Shorts

The papers are in the second divider. They are:

- Flag H - Tom King's paper covering Harland and Wolff and Mackies.
- Flag I - Tom King's paper on Shorts.
- Flag J - Cabinet Office brief on the two papers
- Flag K - George Guise's note covering both papers.

You are already familiar with most aspects of the latest position in these companies, and need only skim Tom King's papers. You should however read George Guise's note (Flag K) and use the Cabinet Office brief (Flag J) to steer the discussion.

The key issues are:

- on Harland and Wolff set a timetable for Tom King to report back on progress in the discussions with the MEBO/Olsen consortium. And settle whether those

Mr Olsen has now written to you. See Plan L. SECRET

d

discussions should be within a financial envelope of £275 million (Tom King's figure) or £220 million (John Major's figure).

- on Mackies: invite a report back in two months, reminding Tom King of the £20 million financial limit.

- on Shorts:
 - Note the position on the capital injection of £390 million.

 - Settle whether negotiations should be on an exclusive basis with Bombardier, or in competition between Bombardier and Fokker/GEC.

 - Whether the negotiations should be within a total ceiling of £600 million.

Rec.

PAUL GRAY
1 March 1989

KAYARV

FRED. OLSEN

CF
L
FRED. OLSENS GATE 2
OSLO 1

February 24, 1989

The Rt. Hon. Margaret Thatcher MP,
Prime Minister,
10, Downing Street,
London SW1.

Dear Prime Minister,

You will know from the Secretary of State, Mr. Tom King, that I have confirmed our commitment to the Management Employee Buy Out of Harland & Wolff by taking a major equity stake and in placing the initial orders for 3 ships.

I have also authorised the MEBO final offer to the Department of Economic Development on February 17, 1989.

I visited the yard after extensive discussion with Dr. John Parker and have met Management and Trade Union representatives. I am satisfied that the key ingredients are present for ultimate success but we will have to work hard and harmoniously to ensure a long term healthy future.

The financial package we have jointly constructed with H&W/Management is based on demanding targets of performance but we believe these to be achievable and Dr. Parker and I intend to hire in Japanese yard consultants to assist us in this task.

The market is improving for new ships and of course in such an international business we will also need good fortune.

I wish to personally assure you of my commitment and enthusiasm to establish a successful privatised Harland & Wolff.

Yours sincerely,

C.c.
Secretary of State for Northern Ireland

Fred. Olsen -



10 DOWNING STREET

LONDON SW1A 2AA

23 February 1989

From the Private Secretary

SUBJECT CC MASTER

Dear Sir,

PRIME MINISTER'S MEETING WITH NORTHERN IRELAND MPs TO
DISCUSS PRIVATISATION OF HARLAND AND WOLFF

The Prime Minister this afternoon met a delegation from the three main political parties in Northern Ireland to discuss the privatisation of Harland & Wolff. The delegation comprised Mr. James Molyneaux and Mr. Roy Beggs of the UUP, Dr. Ian Paisley and Mr. Peter Robinson of the DUP, and Mr. John Hulme and Mr. Austin Currie of the SDLP.

Your Secretary of State and Mr. Viggers were also present.

The members of the delegation spoke in turn. Opening the meeting Mr. Molyneaux expressed gratitude for the Prime Minister's earlier letters and for agreeing to meet the delegation. He said that the delegation did not wish to quibble with the privatisation decision; they wished to co-operate with the Government in ensuring that Harland & Wolff remained a going concern. Northern Ireland was now beginning to benefit from the Government's economic policies, and it would be a tragedy for this to be set back by the closure of its largest employer. The economic significance of Harland & Wolff in Northern Ireland went wider than its Queens Island site; many other jobs in component suppliers in other parts of the Province were also affected. The delegation were particularly encouraged by the proposed takeover of the company by a management and employee buy-out (MEBO) supported by Mr. Fred Olsen.

Mr. Hulme also expressed appreciation that the meeting was taking place. It was an historic occasion; the first time on which representatives of all the Northern Ireland parties had jointly met a United Kingdom Prime Minister on any issue. This joint approach demonstrated the widespread concern in the Province for the future of Harland & Wolff. The delegation hoped that privatisation could be successfully achieved; and would play its part in encouraging future co-operation by the workforce. He believed that the management and workforce of the company were now keen to stand on their own feet and make privatisation work; he hoped the Government would encourage that process by allowing the MEBO to proceed.

Mr. Robinson said he shared the view that this was a unique occasion, which demonstrated the sincerity of all sections of the community about the key role of Harland & Wolff. He had a particular personal interest, as the shipyard was located in his constituency. He believed the MEBO supported by Mr. Olsen offered a secure future for the company; Mr. Olsen had demonstrated his commitment and confidence in the discussions so far, and he hoped the Government could back this up. He believed that the MEBO/Olsen bid would be less costly to the Exchequer than closure. It would be a great encouragement if the delegation was able to leave the meeting with an assurance that an early conclusion would be reached on the sale proposal; this was important in order to stem the loss of morale both amongst Harland & Wolff workers and its customers.

Responding to the last point, your Secretary of State said that the Government was in close discussions with the MEBO. Mr. Olsen's involvement made this a much more significant proposal. These discussions were being pursued urgently, but Northern Ireland Ministers were not yet in a position to put a firm proposal to their colleagues. Assuming that position could be reached, it had to be recognised that a substantial amount of Exchequer support would be involved, and clearance from the European Commission would be necessary. The Prime Minister agreed with this, and said that the Government was keen to adopt a similar approach in these discussions to that employed during the sale of the Govan shipyard to Kvaerner.

Mr. Robinson said that he recognised the need for a substantial injection of finance. But it was encouraging that Mr. Olsen was contemplating an order of perhaps nine to ten ships; the experience gained on the first few ships would mean that a very good productivity record could be achieved as the orders proceeded. Your Secretary of State said that the Harland & Wolff yard was very well equipped and high levels of productivity were within the grasp of the workforce; but the prerequisite had to be a new spirit of motivation and improved efficiency. Mr. Molyneux suggested that members of the delegation might be able to help stimulate motivation amongst the workforce.

Mr. Currie added his thanks for the meeting. He felt that the existence of the united delegation had already had an important impact in raising motivation both in the shipyard and Northern Ireland more generally. He hoped that the new spirit of confidence could receive a further boost from the Government. He believed it was significant that Mr. Olsen was not only a shipowner but had other industrial interests; this had helped to boost confidence amongst the banks. Further encouragement was given by the fact that the management and employees were prepared to make large personal financial sacrifices in supporting the MEBO. He also thought it significant that, during the 25 years he had been active in Northern Ireland politics, he had never until recently received an invitation to visit Harland & Wolff; that this had now occurred showed the substantial change of

attitude that was taking place among the shipyard workers and the population generally.

Mr. Beggs stressed the importance of avoiding the creation of a wasteland in East Belfast; that had occurred in the past in West Belfast and must not be repeated. In supporting the comments of other members of the delegation, he said this was a unique opportunity for the Government to demonstrate that its privatisation policy could bring success in Northern Ireland as elsewhere.

Dr. Paisley said that he had a very personal feeling for the future of the shipyard; he had lived in East Belfast for 45 years and had carried out his pastoral work there. He agreed that the tragedy of West Belfast - which, thankfully, was now being reversed - must be avoided in East Belfast. He said that there had been no tradition in the past of politicians from any party making visits to the shipyard - he personally had only been there on three occasions. He supported the comments of other members of the delegation about Mr. Olsen; he was a well respected person, who would be an ambassador for Northern Ireland across the world, with big spin-off benefits for the Province. At the same time it was important that Mr. Olsen was proposing only to hold a minority of the equity in the company; so control would not be passing out of Northern Irish hands. The employees and management wanted to take on responsibility, and it would be a great thing for the Government to give them its backing. The social consequences of closure would be a tragedy for East Belfast. At the same time he fully accepted that the privatisation package would represent the last injection of Government money; the company could not expect to keep coming back for further support. He stressed the urgency of reaching a decision, but recognised that the Government must be satisfied the structure of a privatisation proposal was right; the one thing that could not be afforded was a failure.

Responding to the comments by the delegation the Prime Minister said that the Government's objective was the privatisation of Harland & Wolff and getting the restructured company off to a good start. But to do that it was necessary to keep those interested in taking over the company keen to do so; and it was the attitude of the management and workforce that would be critical in this rather than that of the Government. Bidders had to be persuaded that the employees would deliver the goods, particularly bearing in mind the unhappy history of the yard. Meantime the Government did need to study proposals in detail, and if it accepted them would need to justify them to the European Commission. Once the company had been privatised, Government support would be limited to Intervention Fund support in line with the EC rules.

Dr. Paisley stressed the importance of successful packaging of any proposal in presenting it to the Commission; he and other colleagues with experience of Europe might be able to help in this. Your Secretary of

State welcomed this offer, and saw considerable attraction in a joint approach to the Commission from Northern Ireland MEPs.

Discussion then turned to current performance at Harland & Wolff. Your Secretary of State said that progress with the BP SWOPS contract was disappointing, but that better progress was being achieved with the AOR. The Prime Minister stressed the importance for privatisation proposals of improving performance on the current contracts. Members of the delegation said that, while they recognised this, it was difficult for the workforce when there was a background of uncertainty; firm orders would bring out the best in the yard, as for example when they completed the Falklands order in 13 weeks. But members of the delegation accepted that they would need to support Ministers' efforts in emphasising to the workforce the importance of achieving new levels of performance both to bring about a successful privatisation and to ensure the continued success of the company in the private sector.

Summing up the discussion, the Prime Minister thanked the delegation for putting forward their views. It was agreed that it should be made clear to the press that a successful meeting had taken place. The line should be that the Government was keen to achieve a successful privatisation of Harland & Wolff supported by an appropriate package, which would be subject to the approval of the European Commission.

Yam,
Paul

(PAUL GRAY)

Stephen Leach, Esq.,
Northern Ireland Office.

PRIME MINISTER

HARLAND AND WOLFF: MEETING WITH NORTHERN IRELAND MPs

You have agreed to meet an all party delegation of Northern Ireland MPs to discuss the future of Harland and Wolff. This follows the delegation's earlier meeting with Tom King on 1 February.

The meeting will take place after Questions. Tom King and Peter Viggers will come at about 1540 to give you a short briefing. The Northern Ireland delegation are then scheduled to come in at 1550.

Briefing is in the folder below. The history and key points are summarised in the letter of 20 February from Tom King's office immediately below. Then there is:

Flag A - Record of the 1 February meeting together with the press release issued afterwards.

Flag B - Detailed briefing on points to make.

The main points on which you will be pressed are:

- The wish for a commitment that closure is ruled out. You will want to go no further than Tom King in stressing that, while every effort is being made to find a private sector solution, this is not yet assured, and no guarantee against closure can be given.
- Why intervention aid on possible new orders is not being given pending privatisation. You will want to stress that, consistently with the policy adopted for British Shipbuilders, the Government is no longer prepared to underwrite losses over and above the general level of assistance within the EC limit.

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There may be pressure for some kind of agreed statement after the meeting. If so, you should resist anything that goes beyond the agreed statement after the 1 February meeting (last page at Flag A).

REC.

PG

22 February, 1989.

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NORTHERN IRELAND OFFICE
STORMONT CASTLE
BELFAST BT4 3ST

Tel. Belfast (0232) 63011

Paul Gray Esq
10 Downing Street
LONDON
SW1A 2AA

20 February 1989

Dear Paul,

PRIME MINISTER'S MEETING WITH NORTHERN IRELAND MPs TO DISCUSS
PRIVATISATION OF HARLAND AND WOLFF

Your letter of 17 February recorded that the Prime Minister has agreed to meet the leaders of the three main political parties in Northern Ireland (and their respective spokesmen on industrial matters), together with the Secretary of State and Mr Viggers, on Thursday 23 February to discuss the privatisation of Harland and Wolff. The UUP will be represented by Mr James Molyneaux and Mr Roy Beggs, the DUP by Dr Ian Paisley and Mr Peter Robinson, and the SDLP by Mr John Hume and Mr Austin Currie. All except Mr Currie are MPs while Messrs Paisley and Hume are also MEPs; the shipyard is within Mr Robinson's constituency.

Mr Molyneaux wrote to the Prime Minister on 14 December 1988 expressing concern about Harland and Wolff and seeking a meeting to be attended jointly by Dr Paisley, Mr Hume and himself, accompanied by the respective industrial spokesmen. The Prime Minister agreed in principle to this request but suggested that it should be preceded by a meeting with the Secretary of State. The Northern Ireland MPs agreed to this (on the basis that the meeting would be preparatory to the one with the Prime Minister); in the event they recognised it as a substantive meeting and presented their case constructively and harmoniously (a note of the meeting on 1 February is at Annex A).

The delegation accepted that the policy was to privatise Harland and Wolff and did not seek any reversal of this. They argued that the company was a vital component of the industrial infrastructure in the Province and questioned the decision not to allow H&W to take orders prior to privatisation. They (and in particular Mr Robinson



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who was the main spokesman) were clearly aware of much of the detail of the different proposals for privatisation and expressed preference for the management/employee buy-out (MEBO). The group pressed the Secretary of State for a statement that closure had been ruled out; but Mr King explained that while every effort was being made in the search for a private sector solution, this was not yet assured and accordingly closure could not be excluded as an option.

The Prime Minister may wish to reinforce the points made by the Secretary of State on 1 February. Briefing notes are attached on current progress on the privatisation of H&W and Government policy on further orders, together with information on the commercial performance of the company, key facts, current workload and recent shipbuilding market forecasts. A schedule of briefing material provided is at Annex B.

The Prime Minister may be pressed on the Government's decision not to provide intervention aid on possible new orders for the shipyard pending privatisation. The bull point here is that, even after intervention assistance from HMG up to the EC limit, all recent ships built by Harlands have made further losses. The Government is no longer prepared to bear the risk of cost overruns on new orders.

In view of the speculation in Northern Ireland that the emergence of Mr Olsen virtually ensures the success of the MEBO and the future of H&W, the Prime Minister will wish to stress that whilst Government is trying hard to secure a viable future for the yard, no guarantee can be given and closure remains an option.

Yours sincerely,

Stephen Leach.

S J LEACH

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JB/PROB/19995

From: PS/Secretary of State (B) cc
7 February 1989

PS/SofS (B&L) - B
PS/Mr Viggers (B&L) - B
PS/Dr Mawhinney (B&L) - B
PS/PUS (B&L) - B
PS/Sir K Bloomfield
Mr Burns - B
Mr Fell, DED
Mr Semple, DFP
Mr Thomas - B
Mr Gibson, DED
Mr Watkins, DFP
Mr Miles - B
Mr G McConnell - B
Mr J McConnell - B
Mr P McDonnell, DED

NOTE FOR THE RECORD

HARLAND & WOLFF: MEETING WITH NORTHERN IRELAND MPS

A delegation consisting of Mr Jim Molyneux MP, The Rev Ian Paisley MP, Mr John Hume MP, Mr Roy Beggs MP, Mr Peter Robinson MP and Mr Austin Currie came to see the Secretary of State and Mr Viggers in NIO(L) on 1 February to discuss Harland & Wolff. Mr G McConnell and Mr McDonnell were also present.

2. Mr Molyneux began by saying that while the group had asked for a meeting with the Prime Minister to follow this one with the Secretary of State (and she had agreed in principle to this) this was not in any sense meant as a slight to the Secretary of State. Because of the significance of Harland & Wolff in Northern Ireland they wished to register their views at the highest level, but they fully recognised that the Secretary of State had prime responsibility for the Yard and therefore expected the present meeting to be the substantive one. (They also of course recognised that the Secretary of State would be at the meeting with the Prime Minister.) The Secretary of State said that he understood the point. The reality was that the Prime Minister and he were indivisible. While it was always her practice to meet MPs who asked to see her, she would be guided by the advice of the relevant Departmental Minister, and this was particularly the case on an issue of such importance as Harland & Wolff. It was therefore

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sensible of the group to see him first, as the Prime Minister had requested them to do. He would report to the Prime Minister after the meeting.

3. Turning to the position at Harlands, the Secretary of State explained that against the background of the Government's decision to privatise the Yard, two proposals were currently being very carefully considered. The first was for a management and employee buy out (MEBO) while the second was for the purchase of the Yard by the management team from Bulk Transport. Intensive work on these options was going on, with Mr Viggers taking a leading role. He was not in a position to say much about the substance of the negotiations at the moment, although it was worth pointing out that the MEBO option was not fully credible as it stood and would need the support of a major industrial or financial partner. There were in fact 2 possible partners who had been mentioned and were being looked at. If either MEBO or BT were proceeded with, there would be substantial work to do in getting the endorsement of the EC for the new arrangements and the united support of the Northern Ireland parties, particularly the MEPs, would be very useful in this context.

4. Mr Paisley thanked the Secretary of State and said that Mr Robinson would take the lead in presenting the group's views. Mr Robinson began by saying that although a number of the Northern Ireland parties did not agree with the philosophy of privatisation, and/or had doubts about the timing of privatising Harlands now without a 'fattening-up' period, he would not pursue these since there was no point in disputing the policy as it now stood. As the breadth of the present delegation showed, Harlands was a key employer in Northern Ireland, providing substantial direct employment, a good deal of other employment in manufacturing and service companies, and offering training in highly skilled work to a large number of young men. The perception which was widely present in the Yard and in Northern Ireland generally was that the Government was preventing Harland & Wolff from acquiring new work and was also spreading negative briefing about the Yard. While the reality might be more complex than this, it could hardly be denied

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that the Government had not been fulsome in its comments on Harland & Wolff and this had really affected morale in the Company and in the community at large.

5. Mr Robinson went on to say that he had spoken both to Mr Pollock of BT and to Mr Parker about the 2 options which were on the table. While both were clearly better than closure, he felt that MEBO offered much better long-term prospects. He was concerned that the fact that the BT option cost less might incline the Government towards it, even though the future it offered for Harlands was in low-tech 'metal-bashing' work, sticking to the large tanker market where competition was in fact greatest. While Mr Pollock was a very personable individual, he suspected that he and his BT colleagues were primarily in the market for the cheap ships which under this proposition they could get built at less than market value. Apart from anything else the EC would surely see through this device. MEBO, on the other hand, seemed to offer a long-term future: Mr Parker was a very able individual who wished to keep the Yard afloat and had a highly perceptive understanding of the world shipping market. The fact that he had now attracted the support of two major possible partners showed that he inspired confidence in people of experience and very substantial resources. As Mr Robinson understood it, one of these potential investors would be willing to place orders with the Yard (thus enabling MEBO to match this important possible feature of the BT proposal).

6. Concluding Mr Robinson said that because of the perception of the Government's hostility and the recent redundancies, morale and productivity at Harlands were now very low. This was hitting the work on SWOPS and other orders. It would be enormously valuable if the Secretary of State could issue a statement - for example after this meeting - stressing the Government's commitment to a viable long-term future for the Yard. Without this, potential customers might be scared off too.

7. The Secretary of State complimented Mr Robinson on this well-informed presentation. Mr Paisley said that he supported the reservations which had been expressed about the BT option.

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Mr Pollock made a virtue of not asking the work force at the Yard to contribute financially, but in fact they ought to be made to contribute so as to have a stake in the success of the privatised Yard. The MEBO option was greatly preferable in this respect.

Mr Currie, Mr Beggs and Mr Hume all briefly expressed their support for Mr Robinson's analysis and argued the case for the work force and suppliers to be given more solid grounds for confidence in the Company's future.

8. The Secretary of State said that he was impressed by the sincerity and unanimity of the delegation. He had worked hard at improving the economic situation in the Province, and there had been a good deal of success; but Harlands and Shorts were the great exceptions. However, he was not in a position to respond at this moment to the delegation's request for an unqualified commitment from the Government to the Yard's future. A great deal of work was going on and there were considerable hurdles to surmount, not least with the EC. He would value the delegation's continuing support. On the 2 options, both had pluses and minuses and the choice was not quite as clear-cut as had been suggested. While the appearance of possible industrial partners for the MEBO option had certainly given it some credibility, the choice was by no means clear-cut. One aspect of BT which should not be lost sight of was that the Company was prepared to place an order for relatively straightforward ships. These might not be particularly high-tech, but a steady dose of regular and efficient serial production of simple snips could well be good news for Harlands. He had nothing against specialist ships, but the complexity inevitably made time and cost overruns more likely; SWOPS was a case in point. A key element in working towards the successful resolution of the Yard's difficulties was to keep the work force actually at work; any form of industrial action would be most damaging. In conclusion, the Secretary of State stressed that he hoped that he would be able to secure a viable future for the Yard but he could not guarantee this. Mr Hume asked whether the Secretary of State could rule out closure as an option. The Secretary of State made clear that he could not do so at the present time. Mr Hume and Mr Paisley then commented on the EC aspect, noting that any package deal put to the Commission would

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have to dwell more on the regional than on the industrial arguments, since the aid envisaged for the Yard could well be outside the normal limits for shipbuilding aid. The Secretary of State commented that this was indeed likely. If a viable way forward could be found it would probably be necessary to clear all the Company's existing liabilities, which would come to several hundred million pounds, and there would then in addition be intervention aid and possible additional subsidies.

9. The meeting then turned to the drafting of an agreed press statement for use after the meeting. This is attached (not to BII's recipients). In conclusion, the delegation thanked the Secretary of State for receiving them. The Secretary of State said that he had found it a constructive and helpful meeting. He would consult the Prime Minister about an appropriate time for a meeting with them (Action: Mr G McConnell for advice please).

Stephen J. Leach

S J LEACH
Private Secretary

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PROB/19618



Northern Ireland Office

Press Notice

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L 11/89

1 February 1989

HARLAND AND WOLFF

The following agreed statement was issued after today's meeting between the Secretary of State and Northern Ireland political leaders.

A delegation consisting of Mr Jim Molyneux MP, the Reverend Ian Paisley MP, Mr John Hume MP, Mr Roy Beggs MP, Mr Peter Robinson MP and Mr Austin Currie today met the Secretary of State for Northern Ireland, Mr Tom King MP and the Industry Minister, Mr Peter Viggers MP to express its serious concern about the future of Harland and Wolff. The Secretary of State assured the delegation that this concern was shared by the Government and made clear that every effort was being made to try to achieve a long term future for the industry. He said that work was proceeding on several definite possibilities that could offer a way forward. The Secretary of State was not yet able to indicate whether the desired objective could be achieved but agreed to keep the delegation informed of significant developments. He will also consult the Prime Minister about an appropriate time for a meeting with the delegation.

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ANNEX B

- Annex B1 : Benefits of Privatisation; Bull Points
- Annex B2 : Key Facts on H&W
- Annex B3 : H&W Commercial Performance in Public
Ownership
- Annex B4 : Current Workload at H&W
- Annex B5 : Position on Negotiations with Private Sector
Interests
- Annex B6 : Negotiations with Tikkoo Cruise Line (TCL)
- Annex B8 : Government Policy on Further Orders and MOD
Orders
- Annex B9 : Redundancies
- Annex B10 : Most recent Market Forecasts

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ANNEX B1

BENEFITS OF PRIVATISATION - BULL POINTS

The Prime Minister may wish to set the privatisation of Harland and Wolff in the context of

- (a) her concern about the future of the company;
- (b) the difficult position of the world shipbuilding industry;
- (c) the need to move quickly towards privatisation;
- (d) the wider benefits of privatisation policy.

Opening points which the Prime Minister may wish to make include:

- Government is as concerned as Northern Ireland MPs about the position of Harland & Wolff. It is in an effort to secure its future that privatisation is being addressed as a matter of urgency.
- Government also recognises the difficult market position which confronts H&W and the world shipbuilding industry. In the last financial year all but one of Japanese shipyards made a loss and Korean shipyards also faced severe financial difficulties (eg Daewoo). Moreover, while the most recent forecasts for shipbuilding predict an upturn in the market in the 1990s, it is clear that any recovery will be slower and less significant than originally anticipated.

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- In very difficult market conditions rapid response is important. Private sector companies are better able to respond to the changing nature of the market place and decision-taking on new orders or new investment than publicly owned companies constrained by issues of public accountability.
- There is no possibility of the Yard remaining in public ownership with Government continuing to underwrite its losses: Ministers are totally persuaded that H&W can only be saved by its return to the private sector. The quicker this can be achieved the better will be H&W's future prospects.
- Public ownership has been no true friend of H&W. In public ownership H&W employment has fallen from 9,500 to under 3,400 and annual losses have been as high as £50m. The need to fund these losses impacts on the needs of other competing programmes within the Northern Ireland public expenditure allocation.
- Government firmly believes in the benefits of privatisation. 17 major businesses with around 655,000 jobs have been returned to the private sector, with most having improved output, employee morale, industrial relations and employment. (Examples: Rolls Royce, Royal Ordnance, Jaguar, National Freight Corporation, Associated Ports). These improvements have been derived from the influence of commercially, ie financially driven disciplines leading to increased productivity and improved efficiency.
- Northern Ireland economy is currently enjoying the benefits of UK Government economic policy based on privatisation and the control of inflation. Recent

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economic indicators show that:

- unemployment has reduced by 24,000 since October 1986
- employment has increased by almost 6,000 since March 1987
- 12,400 IDB job promotions achieved 1985-88, 12,200 LEDU job promotions achieved 1985-88
- Significant recent investments by a number of companies including GEC, Ford, Howden Sirocco, Montupet, Daewoo

H&W's image as an old non-adaptable industry in public ownership does little service to increasingly positive image of the rest of the Northern Ireland economy.

Government is urgently trying to find a solution to the problems of H&W which offer it the best possible future in the private sector.

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ANNEX B2

HARLAND AND WOLFF

SOME KEY FACTS

1. EMPLOYMENT

Total Employment	1960	23,000
	1975	9,500
	1980	7,370
	1986	4,940 (at March)
	1987	4,900 (at March)
	1989	3,310 (at January)

2. TRADING PERFORMANCE	1982/83	1985/86	1986/87	1987/88
	fm	fm	fm	fm
Turnover	72	82	78	68
Loss on Work carried out	20	25	30	43
Total Loss	43	37	76	25

3. CURRENT CONTRACTS

Financial Aspects

SWOPS	Proceeds	£121.1m
	Costs	£164.8m
	Latest estimated loss (December 1988)	£43.7m
AOR	Proceeds	£137.3m
	Costs	£148.9m
	Latest estimated loss (December 1988)	£11.6m

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ANNEX B3

H & W COMMERCIAL PERFORMANCE IN PUBLIC OWNERSHIP

1. Employment has declined from 9500 to 3310: public ownership has not served to protect employment at Harland and Wolff.
2. Despite substantial Government financial support (£485m since 1975) company's financial performance has not improved.
3. After intervention assistance from Government up to the limits allowed by the EC all recent ships have made further losses.
4. Over period 1983-89 H & W received £35.8m in intervention assistance, representing only 15% of total Government funding.

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ANNEX B4

CURRENT WORKLOAD AT H & W

SWOPS

Contract awarded by BP March 1985 lays down two delivery dates

	Contract Date	Latest Forecast Date
Interim Handover (ie ship completed by H & W)	June 1988	November 1989
Final Handover (ie over sub sea well head following successful sea trials and test runs)	Expected to be 6 months later	

Estimated Loss £43.7m
(36.1% of expected proceeds)

Vessel is structurally complete and floating in building dock. Outfit work and commissioning of systems continuing.

AOR (Auxiliary Oil Replenishment Vessel)

Contract awarded by MOD in April 1986.

Contract Delivery Date	October 1990
Latest Forecast Delivery Date	February 1991
Estimated Loss	£11.6 million (8.4% of price)

Keel of vessel laid in building dock August 1988. Over 80% of steel has now been fabricated, pre-outfitting has commenced and the erection of blocks in the building dock is progressing.

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ANNEX B5

CURRENT POSITION ON NEGOTIATIONS WITH PRIVATE SECTOR INTERESTS
(NOT TO BE DISCLOSED)

(a) MANAGEMENT EMPLOYEE BUY-OUT (MEBO)

A proposal was received from the H&W MEBO Team on 23 December. The proposal related to Sealink Ferries or the Ultimate Dream. The MEBO Team were informed that the cost of the proposal was unlikely to be acceptable to Government.

On 2 February Mr Parker, Chairman of H&W, put forward a revised proposal involving Mr Fred Olsen. Mr Olsen would provide equity for the new company, accept a position as Non-Executive Chairman, and order 3 140/150,000 tonne crude/product carriers priced at \$50m each.

Several meetings of DED officials, H&W management and an Olsen representative have been held during the past 2 weeks.

(b) BULK TRANSPORT (BT)

The BT proposal is based on a programme of 3 very large crude carriers (VLCCs) priced at \$75m each.

A further BT proposal is expected on 22/23 February.

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ANNEX B5 (CONT)

2. LINE TO TAKE

The interests involved in the H & W privatisation have requested confidentiality and the Prime Minister is therefore limited in the amount of detailed information which she can provide.

BT have, however, publicly expressed their interest in building VLCCs at H&W and the Prime Minister may wish to confirm that DED and BT, with their respective advisers, are involved in discussions with a view to finalising a business proposal. With regard to the MEBO/Olsen proposals the Prime Minister can confirm that discussions are also continuing although no details can be disclosed at present.

The Prime Minister may also wish to indicate that Government is prepared to negotiate a supportive package to enable a privatisation to go ahead, though any arrangements will be subject to the approval of the EC.

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ANNEX B6

(Not to be disclosed)

NEGOTIATIONS WITH TIKKOO CRUISE LINE

1. The attached table shows a comparison between the TCL proposal and DED's counter proposals.
2. In the end it was not possible to bridge the gap for the following reasons:
 - Mr Tikkoo produced no evidence of commercial funding for the P3000 (either to DED or to ECGD).
 - Mr Tikkoo was not prepared to put any cash into H&W.
 - TCL wanted an up-front payment from Government of £62.5m as working capital and to cover any cost overruns on P3000.

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TIKKOO CRUISE LINE
PROPOSAL AND COUNTER PROPOSALS

	Tikkoo Proposal of 27.7.88	DED Counter Proposal of 16.9.88	DED Improved Proposal of 3.10.88
	£m	£m	£m
1. Intervention Aid on P3000	100 (later £104m)	100	100
2. Grants on unrecovered overheads, surplus capacity costs and future capital expenditure	96.8	35	54
3. Cash Reserve	62.5	-	-
4. Assistance with payments for redundancies in excess of statutory scheme.	Not Quantified	-	10
5. Purchase of assets by Tikkoo Cruise Line	-	(10)	(10)
6. Value of proposal to Tikkoo Cruise Line	259.3	125	154
7. Residual liabilities to be paid by HMG (estimated and excluding £400m write-off of loans)	65.7 <u>325</u>	55 <u>180</u>	55 <u>209</u>

In the end, it was not possible to bridge the gap primarily because:-

- (1) TCL failed to produce (to both the Department and ECGD) satisfactory evidence of commercial funding for the balance required for the P3000 - £270m (line 1);
- (2) TCL wanted an up-front cash payment from Government of £62.5m for unidentified working capital purposes (and as protection against cost overruns on the P3000) (line 3); and
- (3) TCL was not prepared to put any cash at all into Harland & Wolff.

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ANNEX B8

GOVERNMENT POLICY ON FUTURE ORDERS AND MOD ORDERS AND FUTURE MARKET STRATEGY

It is likely that the Prime Minister will be pressed on the Government's decision not to provide intervention aid on possible new orders for Harland & Wolff (Ultimate Dream and the South Coast Shipping dredger order). The question of MOD work and future market strategy for H&W is also likely to be raised. Key points on these issues are provided below.

New Orders

- Government is ready to consider intervention aid on any order (including the Ultimate Dream) on receipt of an application from a new owner of H&W.
- However, it is up to a new owner to be satisfied that figures on which application for intervention assistance is based are sufficient to cover costs. Government is no longer prepared to bear the risk of any cost overruns on new orders.
- Prospective new owners will in any event have their own plans for the Yard and it would be wrong for Government to have encouraged a publicly owned yard to take orders which would have compromised the plans of potential private sector owners.
- While new orders may have boosted company morale in the short-term, it is much more important to achieve a lasting and long-term solution to the Yard's problems.

MOD Orders

- There is no blacklist in respect of MOD work
- All other yards undertaking MOD work in UK are in the private sector. Government wishes to ensure that companies compete

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for defence contracts on the same basic conditions. AOR contract was awarded to H&W in 1986 recognised need to ensure fairness between companies in private and public sectors.

- Once decision was taken to privatise H&W it was clearly better to allow this to happen before awarding new work. It will be open to the yard under private ownership to seek further MOD orders.
- New owners will, however, have their own plans for the Yard and it will be for them to decide whether they wish to seek MOD work. Should they do so they will receive the full support of Northern Ireland Ministers.

Future Strategy

It is possible that the Northern Ireland MPs may argue the company's case against the building of low technology ships such as tankers and bulk carriers because of Far Eastern competition and in favour of the building of more sophisticated ships. Key points which might be made are:

- Company's recent experience of building ships (including sophisticated ATS and SWOPS) has resulted in significant cost overruns. No reason why building more complex ships should result in smaller losses.
- The expected upturn in the shipbuilding market comprehends an increased demand for VLCCs during the next decade. Taken together with reduced shipbuilding capacity worldwide (Japan shipbuilding capacity has been reduced in the interim by 60%, all Swedish shipyards have been closed as have Norwegian yards which have contributed to VLCC production in the past) this suggests that demand for VLCCs in the 1990s may exceed supply.

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- While primary potential VLCC newbuilding capacity rests with Korean yards, increased labour costs and the appreciating won may reduce current cost advantages relative to European shipyards. This may in turn reduce problems with EC 6th Directive.
- H&W facilities were designed to build VLCCs and the Yard should be able to compete provided required improvements in productivity can be achieved.

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ANNEX B9

REDUNDANCIES AT HARLAND & WOLFF

This latest position on H&W redundancies is as follows:

- (i) Total in employment at January 1989 3310
- (ii) Total redundancies announced in August 1988 550
- (iii) Expected employment end March 1989 2990
- (iv) Announcement on 31 January of further 470 redundancies during period 1 April 1989 - 1 December 1989
- (v) Residual employment if above redundancies take effect 2520.

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SHIPBUILDING MARKET FORECASTS

1. The Association of West European Shipbuilders (AWES) has just produced a new report on world shipbuilding demand. It predicts an increase in demand for new ships between now and the year 2000.

2. AWES, which includes Harland & Wolff as a member company, produces regular forecasts of demand for new ships. Forecasts are also produced by the Shipbuilders Association of Japan, and the two are invariably very close.

3. AWES FORECASTS (tonnages in million cgt)

	1984	1988
1984-1990	12.7	-
1990-1995	18.5	12.5
1995-2000	-	16.9

4. The new report does not predict a great upsurge in new building. It defers the upturn that was forecast in 1984, and suggests that the peak new building requirement will be slightly less than was forecast in 1984.

5. In the forecast upturn, the bulk of the tonnage required is to replace tankers and large bulk carriers which came into service in the 1970s.



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File 016

10 DOWNING STREET
LONDON SW1A 2AA

From the Private Secretary

17 February 1989

**HARLAND & WOLFF:
MEETING WITH NORTHERN IRELAND MPs**

Thank you for your letter of 15 February.

The Prime Minister is content to meet the delegation of Northern Ireland MPs and Mr. Currie, together with your Secretary of State and Mr. Viggers. We have now arranged the meeting for 1545 on Thursday 23 February in the Prime Minister's Room at the House of Commons.

I should be grateful if you could make the necessary arrangements with the delegation. It would also be helpful if you could let me have briefing for the Prime Minister's use by next Tuesday, 21 February.

(PAUL GRAY)

S. J. Leach, Esq.,
Northern Ireland Office.

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21512



NORTHERN IRELAND OFFICE
WHITEHALL
LONDON SW1A 2AZ

Prime Minister

I fear that you are committed
by the earlier correspondence to meet him
by the earlier correspondence. Contact for us to seek
delegation. Contact for us to seek
to arrange a meeting before
23 February, as proposed?

Paul Gray Esq
10 Downing Street
LONDON
SW1A 2AA

15 February 1989

Dear Paul

Recd
1/2
Yes Mr

HARLAND & WOLFF: MEETING WITH NORTHERN IRELAND MPs

Following the recent correspondence between the Prime Minister and Mr Molyneaux, the Secretary of State and Mr Viggers met Mr Molyneaux, Mr Paisley, Mr Hume, Mr Beggs, Mr Robinson and Mr Currie on 1 February to hear their concerns on Harland & Wolff. No other issues were discussed.

The meeting was constructive and helpful. The MPs accepted that the policy was to privatise Harland & Wolff and did not seek a reversal of this. However, they argued that there was widespread concern in the Province about the future of the Yard and added that the breadth of their delegation demonstrated this. They argued strongly that the company was a vital component of the industrial infrastructure in the Province and expressed their opposition to the decision not to allow Harland and Wolff to take orders prior to privatisation.

The MPs had clearly been well briefed by John Parker, the Chairman and Chief Executive of the company. They were aware of much of the detail of the various proposals for privatisation and expressed a strong preference for the management and employee buyout led by Mr Parker. The MPs pressed the Secretary of State for a statement that closure had been ruled out as an option.

The Secretary of State said he was impressed by the sincerity and unanimity of the delegation but explained that he could not, at this time, respond to their request for an unqualified commitment to the Yard's future. He asked the MPs to use their influence to encourage the workforce of the company to continue work on the existing orders and not to indulge in protest action which could only damage the chances of a successful privatisation. Mr King told the MPs that he would do his best to secure the future of the Yard although he could not guarantee its survival.

At the end of the meeting the attached agreed statement was issued to the Press.

The Secretary of State was well satisfied with this meeting, which brought the major Northern Ireland parties together to meet him about an industrial issue which is undoubtedly of widespread concern in the Province. In her letter of 30 January to Mr Molyneaux, the Prime Minister offered to meet the MPs after they had discussed the matter with Mr King. Although it is unlikely that they will have much to add to what they have already said, the Secretary of State believes it would be right for the Prime Minister (together with Mr King and Mr Viggers) to agree to meet them soon and if at all possible before the E(A) discussion scheduled for 23 February. There are two reasons for this: first, given the importance of the issue both within Northern Ireland and to Government, there would be advantage in the Prime Minister hearing directly from the MPs and, equally important, for them to appreciate how seriously the matter is taken at the top of Government; and second there would be considerable advantage in the meeting taking place while it is known that final decisions have yet to be taken.

Yours sincerely

 S J LEACH



Northern Ireland Office

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L 11/89

1 February 1989

HARLAND AND WOLFF

The following agreed statement was issued after today's meeting between the Secretary of State and Northern Ireland political leaders.

A delegation consisting of Mr Jim Molyneaux MP, the Reverend Ian Paisley MP, Mr John Hume MP, Mr Roy Beggs MP, Mr Peter Robinson MP and Mr Austin Currie today met the Secretary of State for Northern Ireland, Mr Tom King MP and the Industry Minister, Mr Peter Viggers MP to express its serious concern about the future of Harland and Wolff. The Secretary of State assured the delegation that this concern was shared by the Government and made clear that every effort was being made to try to achieve a long term future for the industry. He said that work was proceeding on several definite possibilities that could offer a way forward. The Secretary of State was not yet able to indicate whether the desired objective could be achieved but agreed to keep the delegation informed of significant developments. He will also consult the Prime Minister about an appropriate time for a meeting with the delegation.

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the department for Enterprise

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nbpm

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Direct line 215 5147

Our ref

Your ref

Date 22 December 1988

John Lister

BRITISH SHIPBUILDERS

You will be pleased to learn that, following my announcement on 7 December that no one had been found who offered a viable future for the shipbuilding yards on the Wear, the terms of our proposed closure aid to the yard, including the remedial measures to be arranged through British Shipbuilders, have been successfully notified to the European Commission. The disposal terms of the smaller BS facilities - Clark Kincaid, Appledore, and Ferguson - have also been cleared.

BS hope it will be possible to complete the sale of Clark Kincaid on 23 December. The terms notified for Appledore and Ferguson allow scope for final negotiation and your agreement before completion, but early Commission clearance means that any delay will now be avoided if successful deals can be reached. Progress on Appledore is very encouraging although there may yet be difficulties with Ferguson.

On NESL, the Shipbuilding Unions and local representatives have accepted British Shipbuilders' proposed arrangements for redundancies and an orderly rundown of the yards. John Lister needed the discretion you agreed but made clear it was strictly

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the department for Enterprise

limited to NESL. It is now my intention to press ahead as quickly as possible with the implementation of the agreed package of remedial measures for Sunderland.

I am sending copies of this letter to the Prime Minister, Norman Fowler, Tom King, Nicholas Ridley and Malcolm Rifkind, and to Sir Robin Butler.

*Most grateful
for your help
over this.*

W. King

TONY NEWTON

DE5AAD

NAT IND: Shipbuilding

Pg 15

North East Shipbuilders Ltd.

3.30 pm

The Chancellor of the Duchy of Lancaster and Minister of Trade and Industry (Mr. Tony Newton): With permission, Mr. Speaker, I wish to make a further statement about British Shipbuilders.

In my previous statement on 14 November I was able to report good progress towards a successful sale of most of the remaining elements of British Shipbuilders, following that of Govan earlier in the year. That progress has continued. Agreement is now close for the sale of Clark Kincaid in Greenock and of the Appledore yard in north Devon, and negotiations for the sale of the Ferguson yard at Port Glasgow are under way.

I can additionally report today that I have accepted British Shipbuilders' advice that the preferred bidder for Marine Design Consultants should be the team led by the managing director. Subject to securing further new orders, its bid envisages work being continued in both its Sunderland and Dundee offices. I have asked British Shipbuilders to press ahead with detailed negotiations.

As I said on 14 November, the yards and other facilities that I have mentioned account for five of the six owned by BS, and nearly two thirds of those employed by them, when the process of seeking private sector purchasers was started by my predecessor last April.

The remaining undertaking is, of course, North East Shipbuilders Ltd. at Sunderland.

On 14 November I told the House that, although none of the original bids for NESL had proved acceptable, BS had received three new expressions of interest. To allow time for those to be explored, I was therefore giving until the end of November to establish whether proposals could be developed that gave a firm basis for negotiation. That would entail a clear statement of the work envisaged for the yards, evidence of the technical and financial capacity of the bidder, and the prospect of arrangements likely to be compatible with the European Community sixth directive concerning state support for shipbuilding.

In the event, two of those who had expressed interest prior to 14 November did not submit proposals. The third did so, and two other new proposals also came forward. All three have been carefully considered by British Shipbuilders and its independent financial advisers, against the criteria that I set out.

As a result of that examination, British Shipbuilders' clear advice to me is that none of these proposals could form the basis of a viable future for merchant shipbuilding in the Sunderland yards. None provides evidence of sufficient financial resources, given the major uncertainties of the shipbuilding market. None gives evidence of sufficient work for the future.

Mr. Bob Clay (Sunderland, North): Nonsense.

Mr. Newton: All would entail levels of subsidy which, in one case in particular, could have faced difficulties under the sixth directive.

Mr. Clay: This is an utter disgrace.

Mr. Newton: Reluctantly, and with great regret, I therefore—[*Interruption.*]

Mr. Speaker: Order.

Mr. Bob Cryer (Bradford, South): The right hon. Gentleman is sacking people. How can we remain silent?

Mr. Speaker: Order.

Mr. Newton: Reluctantly, and with great regret, I therefore have to tell the House that I see no further realistic prospect of maintaining NESL in its present form, and its shipbuilding yards will therefore progressively close as the current workload runs out. [*Interruption.*]

There remain possibilities, which I have asked—[*Interruption.*]

Mr. Speaker: Order. Those hon. Gentlemen who have points to make may make them from a standing position when they are called.

Mr. Newton: There remain possibilities, which I have asked BS to make every effort to explore, of selling Sunderland Forge Services, which currently employs nearly 400 people, and interest has also been expressed in one of the yards for purposes other than shipbuilding.

Both my predecessors and I have made it clear that, should it not prove possible for shipbuilding to continue on Wearside, we would bring forward a range of measures to assist those affected and to promote alternative employment in the town.

There will be three main elements. First, we propose a new enterprise zone for Sunderland. [*Interruption.*]

Mr. Speaker: Order. Let us have the details.

Mr. Newton: As with existing zones, this would mean relief from rates for 10 years for all new developments, a simplified planning regime to help speed up such developments, and 100 per cent. capital allowances on new industrial and commercial development. My right hon. Friend the Secretary of State for the Environment is urgently undertaking the necessary consultations with the European Commission and will give details as soon as possible.

Secondly, I have asked English Estates to start work immediately towards the early provision of over £7 million of advance factory space, over and above its existing commitments in the north-east. This will provide around 220,000 sq ft of high quality factory space for new or expanding businesses.

Thirdly, some £10 million will be made available over the next three years for a programme of measures to encourage new enterprise and employment opportunities in Sunderland. About half will be used to give financial support to new or expanding businesses. The other half will be used to assist the present employees of NESL to develop new skills and find new jobs. My right hon. Friend the Secretary of State for Employment will provide services on the shipyard site to advise the work force on opportunities for jobs and training, including help for those who wish to apply for immediate retraining.

Taken together, the measures that I have announced have a total cost of some £45 million. They will significantly reinforce what is already being done to promote economic development in the area through the enterprise initiative, regional assistance, and the work of the Tyne and Wear urban development corporation, which will itself be announcing a number of new projects shortly as a result of the additional funding of £11 million

[Mr. Newton]

announced on 25 November. I hope, that they will also further support and encourage the private sector initiatives that are under way or being considered.

The House will share my regret that, despite every effort, it has not proved possible to find a way forward for NESL. But it must now be right to concentrate on securing a new industrial future for the town, and I believe that we shall have the support of the House in what I have announced to that end.

Mr. John Garrett (Norwich, South): The Minister may talk about the failure of bids for NESL, but the fact is that he has just announced a devastating closure. Is the Minister aware that, for no reason other than dogma, he has just announced the destruction of the Sunderland economy and the death of British merchant shipbuilding? What does he think of his Government's Christmas present for families in Sunderland?

Does the Minister accept that this announcement is humiliating evidence of his failure to reverse the policies of his boss? Does he understand that this act of industrial vandalism not only brings to an end 600 years of shipbuilding on the Wear but destroys an essential British industry with a major contribution to make to our industrial and trading future?

Why has privatisation been given priority over the urgent practical need to secure vital orders? Why have months been wasted in finding private owners when all efforts should have been concentrated on obtaining the orders that would have safeguarded the yard's future? Why is the Government's obsession with the dogma of private ownership so much more important than the thousands of jobs on Wearside and the survival of a great British industry?

Why has the Minister ignored the incontrovertible evidence of an upturn in world shipping demand? Why has he chosen this moment to deliver the fatal blow, just when orders are becoming available and this modern and efficient yard is well placed to take advantage of the upturn?

Does the right hon. Gentleman agree—he did not mention this—that a Cuban order worth at least £110 million is available now and that it would secure the future of the yard? Does he further agree that Britain has already sacrificed more shipbuilding capacity than any other EEC country? Does he agree also that this will mean a total loss of about 5,000 jobs in an area of 20 per cent. unemployment and the loss of skills and experience that are essential to the Sunderland community and the nation?

As for the proposed grants, why is the right hon. Gentleman making unemployment worse before doing something about it? Does this event not add to the record of DTI incompetence? Is it not yet another example of a privatisation bungle, along with that of Girobank and the National Engineering Laboratory? Will he even now think again, swallow his prejudices—or rather, those of his master in another place—and concentrate on providing a future for Wearside and British merchant shipbuilding?

Will the Chancellor also reflect on the contrast between the Prime Minister's warm concern for the threatened workers at the Gdansk shipyard and the callous treatment of Sunderland—or does that explain his prevarication? Will he tell the noble Lord from us that this closure is a wilful act of destruction?

Mr. Newton: Far from dogmatically pursuing a particular policy, we have sought to overcome the problems left behind by a period in which British Shipbuilders, as a nationalised concern, has cost the taxpayer almost £2 billion, including losses of about £650 million, of which at least £100 million was lost by NESL in the past three years merely by fulfilling contracts to build ships.

Against that background, it was clear to my predecessor and to me that a solid future for the yards depended on finding new owners who could run them in a viable way. We are on the verge of succeeding in doing that, as I said in my statement, for five out of the six undertakings owned by British Shipbuilders at the outset of the process, covering about two thirds of the work force.

It is a great and genuine regret to me that we have not managed to find a comparable solution for NESL, and it would be manifestly unfair to the people of Sunderland to pretend that proposals that are manifestly not viable, are viable. I am not prepared to bank on hopes of an upturn in world shipbuilding, which are constantly being revised downwards and which have been further revised downwards in the past few months by the Association of West European Shipbuilders, which suggests that any real upturn will come at best in the latter half of the 1990s, not in the first half as it predicted before.

No one can dispute the fact that if £2 billion had been spent in the past 10 years on providing alternative employment rather than on propping up this industry to make losses we should now be in a better position. I have decided that the right thing to do is to end the uncertainty with the statement I have made this afternoon, and to get on with the job of building a new future for Sunderland.

Mr. Michael Grylls (Surrey, North-West): Does my right hon. Friend accept that his statement detailing the successful privatisation of five of the six remaining yards will bring comfort to those five yards, which will have a more secure future in the private sector? Obviously, for NESL this is a sad day, but will my right hon. Friend remind the company that Corby also had a sad day when the steelworks closed? Today, it is a thriving town with many different firms, large and small. British Steel Corporation (Industry) Ltd. the subsidiary of the then state-owned British Steel, made great efforts to bring new firms to Corby. What was done in Corby can be done in Sunderland, and I am sure that it can be with the help of the measures that my right hon. Friend has announced.

Mr. Newton: My hon. Friend speaks about what has happened in Corby. Consett is another example of a place where comparable proposals have been brought forward to seek to create secure employment for the future. They have met with immense success in recent years and I am determined that we shall have a similar success in Sunderland.

Mr. Chris Mullin (Sunderland, South): Sunderland has been murdered today, in the same way as Jarrow was murdered by a predecessor Government in 1934. Before today's announcement, male unemployment in Sunderland was running at over 20 per cent. There are whole streets where almost no one is working and generations of children are growing up who may never work. This closure was not inevitable. Orders could have been obtained—the Cuban order for example—but no

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the department for Enterprise

cc PAB
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P.O.

The Rt. Hon. Tony Newton OBE, MP
Chancellor of the Duchy of Lancaster and
Minister of Trade and Industry

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✓ Press.
DTC

Miss Carys Evans
Private Secretary to the
Chief Secretary
HM Treasury
Treasury Chambers
Parliament Street
LONDON SW1P 3AG

for

Department of
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Prime Minister

Statement now scheduled for

tomorrow

press

6/12

ms

Direct line
Our ref
Your ref
Date

215 5147

6 December 1988

Dear Carys,

BRITISH SHIPBUILDERS

Many thanks for your letter of earlier today giving the Chief Secretary's comments on the draft statement which the Chancellor of the Duchy anticipates making tomorrow.

You asked to see a revised draft, which I am enclosing. It has not, however, been approved by the Chancellor who is out of London on a regional visit today.

I am still awaiting comments from Clive Norris at DEmp, particularly on the elements of the remedial measures concerning new employment opportunities and training.

I am copying this letter as before.

Yours sincerely,
Peter

PETER SMITH
PRINCIPAL PRIVATE SECRETARY

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CONFIDENTIAL

STATEMENT ON BRITISH SHIPBUILDERS

Mr Speaker, with permission I wish to make a statement on progress in returning British Shipbuilders to the private sector.

I reported progress to the House on 14 November. Since then I have accepted British Shipbuilders' advice that the preferred bidder for Marine Design Consultants should be the team led by the Managing Director. Depending on progress with possible new orders, their bid envisages work being carried on at both Sunderland and Dundee. I have asked British Shipbuilders to commence detailed negotiations with a view to satisfactory completion as soon as possible.

I can also report further progress with privatisation of other facilities. British Shipbuilders are expected to reach final agreement with the management team at Clark Kincaid in Greenock this week for the sale of this facility. BS are also close to reaching final agreement with Langham Industries for the purchase of the Appledore yard in North Devon. Finally, negotiations between British Shipbuilders and Ailsa Perth Limited for the sale of the Ferguson yard at Port Glasgow will begin this week. These disposals will all be subject to clearance with the European Commission which I am confident we shall obtain.

Mr Speaker, I now turn to North East Shipbuilders Limited at
Sunderland.

I announced on 14 November that none of the four bids that had been received at that time was acceptable but that British Shipbuilders had recently received three new expressions of interest. To provide time for these to be explored and for any other interests to be made known, I said that we wanted to establish, by the end of November, whether proposals could be developed which gave a firm basis for negotiation. I explained this would entail a clear statement of the work envisaged for NESL, evidence of the technical and financial capacity of the bidder, and the prospect of arrangements likely to be compatible with the European Community Sixth Directive concerning state support for shipbuilding.

The three expressions of interest prior to 14 November have now been fully explored. Two of the parties concerned decided that, in the event, they were not sufficiently interested to submit a proposal that could be developed to provide a firm basis for negotiation. The third party, however, undertook further work and submitted a proposal to British Shipbuilders. In addition, British Shipbuilders received two new proposals.

British Shipbuilders and their financial advisers have looked carefully at these three proposals. In particular, they have considered them against the criteria I set out in my previous statement. None of the proposals provide evidence that sufficient financial resources would be brought to bear to make a success of the business given the major uncertainties of the world shipbuilding market. Nor has BS been provided with evidence of sufficient work to ensure proper loading for more than a limited period ahead. For these reasons, the advice given to me by British Shipbuilders is clear, that none of these proposals could form the basis of a bid which might prove satisfactory on financial or commercial grounds and offer the viable future for merchant shipbuilding in the Wear that we have always insisted should be found. All of these proposals would also have required a significant degree of subsidy which in one case in particular would have been highly unlikely to have been permitted under the Sixth Directive.

Mr Speaker, I have therefore had to conclude that these latest proposals have to be rejected.

I have previously agreed to two extensions of the bidding period since the first closing date of 30 September since in both cases there had been expressions of interest which could possibly have formed a reasonable basis for negotiation. There are no longer

any such expressions of interest. It is with great regret therefore that I have concluded there is no justification for continuing to seek to privatise the NESL facilities as a single unit.

Mr Speaker, both my predecessor and I have made clear that, should it not prove possible to secure the continuation of shipbuilding in Sunderland, the Government would bring forward a range of measures to promote a new industrial future for the town. I am today able to announce a package of four new measures with a total cost of approximately £43m.

The first of these is a proposed new Enterprise Zone in Sunderland, with a gross cost of approximately £25m. My Rt Hon Friend the Secretary of State for the Environment is urgently consulting the European Commission on this. He will be announcing details as soon as possible. The terms of the Enterprise Zone will be the same as those that have been successfully introduced for similar zones elsewhere, notably:

- relief from rates for 10 years for all new developments;
- a greatly simplified planning regime which cuts through the red tape;

- 100% capital allowances on new industrial and commercial development.

My Rt Hon Friend is seeking to ensure that the new Enterprise Zone will become fully operational as soon as possible. The Government will ensure that it is fully publicised and that companies seeking a place to locate or expand will be given every encouragement to look to Sunderland. This in itself should provide a further major boost to the local economy. In particular it should provide a valuable complement to the existing Tyne and Wear Development Corporation. The Development Corporation itself will be announcing further new projects shortly.

Second, the Government will fund a substantial further programme to stimulate new employment. At least £10m will be made available over the next three years for this purpose. This will be specifically targeted towards assisting the present employees of NESL and to encourage enterprise and new employment opportunities within the Borough of Sunderland.

The third element of the package is also in support of our objective of stimulating new employment. I have requested English Estates to start work immediately towards the provision of at least £7½m of factory space for new or expanding businesses. This is over and above English Estates' existing

commitments in the North East. In addition to encouraging the expansion of businesses in Sunderland, this will also help to alleviate the current shortage of factory space which in itself is a sign of an improving economy.

Fourthly, the Government will take immediate steps to help the workforce of NESL to develop their skills and find new jobs. My Rt Hon Friend the Secretary of State for Employment will provide services on the NESL shipyard site to advise members of the workforce on new opportunities. This will include advice on training. For its part, British Shipbuilders will make every effort to ensure that all of its apprentices are able to find employment with other firms in the area.

My own Department also stands ready to target its promotion of the Enterprise Initiative with the aim of maximising take-up of these opportunities to increase enterprise and employment. In addition to support for consultancy, exports and innovation, Sunderland qualifies for Regional Selective Assistance and Regional Enterprise Grants.

Mr Speaker, I am aware from my several recent visits to the North East that there has been a huge increase already in the prosperity of the North East. This is apparent not just from major inward investment projects such as the Nissan factory, Komatsu and Gold Star but also the many other companies that

have chosen to locate in the North East. The private sector is now playing a key role in maintaining this increasing level of prosperity. Several groups of businessmen are already active in Newcastle. I understand that there are similar groups in Sunderland and Teesside which hope to make announcements shortly. The Government is fully prepared to support and work with such groups.

Mr Speaker, the decision I have announced today has not been an easy one. I have previously made clear to the House that I was determined that every avenue should be explored in trying to find an acceptable bidder for NESL. We have now done that and I have explained why, regrettably, none of the proposals was acceptable. That is now the past and we must look to the future.

I have visited the North East twice in the last few weeks and have seen for myself some of the major new developments taking place. There is a new spirit and sense of confidence in the area. I firmly believe that the new measures I have announced today and the clear commitment of the private sector will build on that and will indeed secure a new future for Sunderland.

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cc: PU.
Press
PAB.
Q
D/C

Department of Employment
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Secretary of State

Peter Smith Esq
Principal Private Secretary to the
Chancellor of the Duchy of Lancaster and
Minister of Trade and Industry
1-19 Victoria Street
LONDON
SW1H 0ET

6 December 1988

Dear Peter,

BRITISH SHIPBUILDERS

...I attach an amplified contribution for inclusion in the Chancellor's statement on British Shipbuilders (your letter of 2 December to Carys Evans refers). This latest version provides a link with this Department's plans for local training arrangements as outlined in our White Paper which we have just published.

I am copying this to Paul Gray (No 10) Carys Evans (Chief Secretary to the Treasury's Office), Roger Bright (DoE), Alison Smith (Lord President's Office) and to Steve Loveman and Trevor Woolley at the Cabinet Office.

Yours sincerely,

Clive Norris

CLIVE NORRIS
Principal Private Secretary



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Employment Department - Training Agency
Health and Safety Executive - ACAS

BRITISH SHIPBUILDERS STATEMENT : EMPLOYMENT DEPARTMENT GROUP
CONTRIBUTION

The Government will also take immediate steps to help the workforce of NESL to develop their skills and find new jobs. My Rt Hon Friend the Secretary of State for Employment will provide services on the NESL shipyard site to advise members of the workforce on opportunities available for jobs and training. This will include help for individuals who wish to apply for immediate re-training. I am also confident that in due course the proposals for Training and Enterprise Councils which my Rt Hon Friend [the Secretary of State for Employment] announced on Monday 5 December will enable the private sector to play a more direct and prominent part in providing the skills required for Sunderland's economic development.

cc/o.



Treasury Chambers, Parliament Street, SW1P 3AG

Peter Smith Esq
 Private Secretary to the
 Chancellor of the Duchy of Lancaster
 Department of Trade and Industry
 1 - 19 Victoria Street
 London
 SW1H 0ET

NBM

RCCG

6/12

6 December 1988

Dear Peter

BRITISH SHIPBUILDERS

Thank you for your letter of 2 December enclosing a draft statement on British Shipbuilders.

The Chief Secretary is generally content with the draft announcement subject to the following points. The draft refers to a total cost of the remedial measures of some £50 million. I understand this comprises the £18 million package agreed during the Survey together with an estimate of £25-30 million for the gross cost of the enterprise zone (the net public expenditure cost of which is to be absorbed within existing provision). This seems rather high. Figures supplied by officials of the Department of the Environment earlier in the year suggested a central value of £23 million. Even making an allowance for possible higher site costs associated with redefinition of the area to include some of the shipyard sites, a figures of £25 million would seem more appropriate, giving a total of some £45 million allowing for rounding up. It would be helpful to indicate in your statement that this overall figure would not be adding to total public expenditure by inserting at the end of the first full paragraph on page 4 'within the announced public expenditure plans'.

The draft announcement does not refer to expected outputs from the expenditure on the remedial measures, e.g. in terms of the amount of factory provision by English Estates, which could helpfully be referred to if available. You might also wish to consider with DOE whether it would be useful to refer to the existing work of the Tyne and Wear Development Corporation in the penultimate paragraph.

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NAT IND Shipbuilding p 15
CONFIDENTIAL

Finally the Chief Secretary sees it as essential that the statement makes clear that the terms of the proposed Enterprise Zone in Sunderland are standard Enterprise Zone terms.

I understand that Mr Newton's announcement has been postponed until Wednesday. I should be grateful if we could see the revised draft statement before it issues.

I am copying this letter to Paul Gray (No. 10) Alison Smith (Lord President's Office) Clive Norris (Department of Employment), Roger Bright (Department of Environment) and to Steve Loveman and Trevor Woolley in the Cabinet Office.

Yours ever
Cans

MISS C EVANS
Private Secretary



re PU

DA

10 DOWNING STREET

LONDON SW1A 2AA

From the Private Secretary

5 December 1988

Dear Pete,

BRITISH SHIPBUILDERS

The Prime Minister has seen your letter of 2 December to Carys Evans, and is content with the proposal for the Chancellor of the Duchy to proceed with an early statement.

I am copying this letter to Carys Evans (Chief Secretary's Office), Alison Smith (Lord President's Office), Clive Norris (Department of Employment), Roger Bright (Department of the Environment), and to Steve Loveman and Trevor Woolley (Cabinet Office).

Yan,
P/G

(PAUL GRAY)

Peter Smith, Esq.,
Department of Trade and Industry.

SW

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the department for Enterprise

cc/lu

CONFIDENTIAL

The Rt. Hon. Tony Newton OBE, MP
Chancellor of the Duchy of Lancaster and
Minister of Trade and Industry

Miss Carys Evans
Private Secretary to the
Chief Secretary
HM Treasury
Parliament Street
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Fax 01-222 2629

Prime Minister

Direct line
Our ref
Your ref
Date

215 5147

2 December 1988

The inevitable outcome. Contact for
Mr. Newton to proceed with a
closure statement early next week?

Yes
PR 6
mt 2/12

Dear Carys,

BRITISH SHIPBUILDERS

You will recall that the Chancellor of the Duchy announced in the House on 14 November that he was prepared to agree to one last effort being made to try to find a viable way forward for North East Shipbuilders Limited. Specifically, he said he wanted to established whether there were proposals that could be developed to provide a firm basis for negotiation for the yard against certain criteria, notably future workload, evidence of technical and financial capacity, and the prospect of arrangements likely to be compatible with the European Community Sixth Directive.

The Department has been advised informally by the BS Chairman, John Lister, that none of the proposals that have been submitted provide an acceptable basis for negotiation on commercial or financial grounds. DTI officials have also established that the one proposal that is at all worked out would be highly unlikely to be permitted under the Sixth Directive. I understand your officials are aware of the background.

The Chancellor has therefore concluded that, on the basis of all the information received so far, the proposals should be rejected. He also feels there is no case for any further extension of the period for new proposals to be put forward.

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Further discussions and consideration of the proposals are currently taking place. Unless, however, there are any significant changes, the Chancellor intends to announce his decision to the House on Monday 5 December. I attach a draft Statement which the Chancellor will be considering over the weekend. I should be grateful for any comments from you and copy recipients as soon as possible on 5 December.

The Chancellor will be writing separately on 5 December about a closure bonus for the workforce at NESL. He hopes the Chief Secretary will consider this sympathetically in view of the difficult industrial relations position at NESL and the announcement he expects to make.

I am copying this letter to Paul Gray (No 10), Alison Smith (Lord President's Office), Clive Norris (D/Em) and Roger Bright (DoE) and to Steve Loveman and Trevor Woolley at the Cabinet Office.

Yours sincerely,



PETER SMITH
PRINCIPAL PRIVATE SECRETARY

STATEMENT ON BRITISH SHIPBUILDERS

Mr Speaker, with permission I wish to make a statement on progress in returning British Shipbuilders to the private sector.

I reported progress to the House on 14 November. Since then I have accepted British Shipbuilders' advice that the preferred bidder for Marine Design Consultants should be the team led by the Managing Director. Depending on progress with possible new orders, their bid envisages work being carried on at both Sunderland and Dundee. I have asked British Shipbuilders to commence detailed negotiations with a view to satisfactory completion as soon as possible.

I can also report further progress with privatisation of other facilities. British Shipbuilders are expected to reach final agreement with the management team at Clark Kincaid in Greenock this week for the sale of this facility. BS are also close to reaching final agreement with Langham Industries for the purchase of the Appledore yard in North Devon. Finally, negotiations between British Shipbuilders and Ailsa Perth Limited for the sale of the Ferguson yard at Port Glasgow will begin this week. These disposals will all be subject to clearance with the European Commission which I am confident we shall obtain.

Mr Speaker, I now turn to North East Shipbuilders Limited at Sunderland.

I announced on 14 November that none of the four bids that had been received at that time was acceptable but that British Shipbuilders had recently received three new expressions of interest. To provide time for these to be explored and for any other interests to be made known, I said that we wanted to establish, by the end of November, whether proposals could be developed which gave a firm basis for negotiation. I explained this would entail a clear statement of the work envisaged for NESL, evidence of the technical and financial capacity of the bidder, and the prospect of arrangements likely to be compatible with the European Community Sixth Directive concerning state support for shipbuilding.

The three expressions of interest prior to 14 November have now been fully explored. Two of the parties concerned decided that, in the event, they were not sufficiently interested to submit a proposal that could be developed to provide a firm basis for negotiation. The third party, however, undertook further work and submitted a proposal to British Shipbuilders. In addition, British Shipbuilders received two new proposals.

British Shipbuilders and their financial advisers have looked carefully at these three proposals. In particular, they have considered them against the criteria I set out in my previous statement. None of the proposals provide evidence that sufficient financial resources would be brought to bear to make a success of the business given the major uncertainties of the world shipbuilding market. Nor has BS been provided with evidence of sufficient work to ensure proper loading for more than a limited period ahead. For these reasons, the advice given to me by British Shipbuilders is clear, that none of these proposals could form the basis of a bid which might prove satisfactory on financial or commercial grounds and offer the viable future for merchant shipbuilding in the Wear that we have always insisted should be found. All of these proposals would also have required a significant degree of subsidy which in one case in particular would have been highly unlikely to have been permitted under the Sixth Directive.

Mr Speaker, I have therefore had to conclude that these latest proposals have to be rejected.

I have previously agreed to two extensions of the bidding period since the first closing date of 30 September since in both cases there had been expressions of interest which could possibly have formed a reasonable basis for negotiation. There are no longer

any such expressions of interest. It is with great regret therefore that I have decided that the NESL facilities will have to close.

Mr Speaker, both my predecessor and I have made clear that, should it not prove possible to secure the continuation of shipbuilding in Sunderland, the Government would bring forward a range of measures to promote a new industrial future for the town. I am today able to announce measures with a total cost of some £50m.

The first of these is a proposed new Enterprise Zone in Sunderland. My Rt Hon Friend the Secretary of State for the Environment is urgently consulting the European Commission on this. He will be announcing details as soon as possible. The Enterprise Zone will provide for:

- relief from rates for the next 10 years for all new developments;
- a sympathetic planning regime which cuts through the red tape;
- 100% capital allowances on all new industrial investment.

Subject to Commission approval, the new Enterprise Zone should become fully operational early in the New Year. The Government will ensure that it is fully publicised and that companies seeking a place to locate or expand will be given every encouragement to look to Sunderland. This in itself should provide a further major boost to the local economy.

The Government will fund a substantial further programme to stimulate new employment. At least £10m will be made available over the next three years for this purpose. This will be specifically targeted towards assisting the present employees of NESL and to encourage enterprise and new employment opportunities within the Borough of Sunderland. I hope to be able to increase this provision under the terms of the European Community Renaval Programme. We are discussing this urgently with the European Commission.

In support of our objective of stimulating new employment, I have requested English Estates to start work immediately towards the provision of at least £7½m of factory space for new or expanding businesses. This is over and above English Estates' existing commitments in the North East. In addition to encouraging the expansion of businesses in Sunderland, this will also help to alleviate the current shortage of factory space which in itself is a sign of an improving economy.

The Government will also take immediate steps to help the workforce of NESL to develop their skills and find new jobs. My Rt Hon Friend the Secretary of State for Employment will provide services on the NESL shipyard site to advise members of the workforce on new opportunities. This will include advice on training.

My own Department in addition stands ready to target further support on Sunderland from the Enterprise Initiative including Regional Enterprise Grants.

Mr Speaker, I am aware from my several recent visits to the North East that there has been a huge increase already in the prosperity of the North East. This is apparent not just from major inward investment projects such as the Nissan factory and Komatsu but also the many other companies that have chosen to locate in the North East. The private sector is now playing a key role in maintaining this increasing level of prosperity. Several groups of businessmen are already active in Newcastle. I understand that there is a similar group in Sunderland that hopes to make an announcement shortly. The Government is fully prepared to support and work with such groups.

Mr Speaker, the decision I have announced today has not been an easy one. But not only are there already major new developments in the area, there is also a new spirit and sense of confidence. I firmly believe that the new measures I have announced today and the clear commitment of the private sector will indeed secure a new future for Sunderland.

070
PRIME MINISTER

HARLAND S. WOLFF

We are due to discuss H&W at E(A) tomorrow.

I have been having further meetings with the management/employee buy-out (MEBO) team, headed by John Parker. We are exploring ways to link a buy-out to a potential order for Sealink, and of dealing with the difficulties of timing which arise because a contract with Sealink may not be possible until mid-1989. One option, which I would like to discuss at E(A) on 1 December, is to develop a MEBO in a phased way.

John Parker has put forward the possibility that the MEBO team establish a new (private sector) company to compete for a small dredger order valued at some £11m. South Coast Shipping had sought to place this order with H&W but it was turned away because we would not make intervention aid available while the Yard remained in public ownership. If the new company were successful in securing the order, it would form the basis on which a fully fledged privatisation could be built, in phases, through the 2 rail-ferries which Sealink want, and which would be contracted in the Spring, the existing contracts for SWOPS and AOR and, eventually, the series of 5 larger Sealink ferries.

There are obvious difficulties, but a successful, if unorthodox, phase 1 privatisation would have major benefits. The privatisation process would be seen to have taken a substantive step forward, Government could confirm (at no great cost) its readiness to provide intervention support (£2½/3m) to a privatised company, morale at the yard would be improved, and construction of SWOPS and AOR proceed without the costly delays which might otherwise result. This latter point is likely to become increasingly important.

NBPM
(Tabled on in today's
E(A) discussion.)

REC
1/12

The difficulties relate mainly to the provision of funding which will equate to a performance guarantee. As I have made clear in my Memorandum to E(A) colleagues, it is not my intention to provide a performance guarantee to any full scale MEBO which might develop. I would therefore impress upon John Parker that what I am now proposing for the dredger order would not be a precedent. I need to encourage the MEBO team to proceed and this provides a relatively low cost means of doing so - and it has the other benefits described above. Effectively I would be providing cover for cost overruns, but on such a small order this should not be significant. Furthermore, the dredger order would be completed well before the projected date of completion of AOR, and would not therefore artificially prolong the life of the operation. I intend, of course, that the costs to Government of any privatisation would be kept within the costs of closure of the yard.

I would aim to seek colleagues' agreement to this proposal at E(A) tomorrow. We are operating to a tight deadline, since tenders for the dredger order must be placed by Noon on Friday, 2 December.

I am copying this minute to E(A) colleagues and to Sir Robin Butler.

TK

30 November 1988

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PRIME MINISTER

JAMES MACKIE AND SONS LIMITED, HARLAND AND WOLFF PLC
AND SHORT BROTHERS PLC
E(A)(88)50

DECISIONS

1. Mr King is still hopeful of selling Mackies to Howdens. But there has been relatively little progress in resolving the future of Harland and Wolff since E(A) last discussed the company on 6 October. The same applies to Shorts whose financial performance has deteriorated still further (Mr King thinks its External Financing Requirement this year could well be £125 million compared with the Board's forecast of £70 million reported in October). The main issue is how much longer Mr King should continue to pursue the privatisation of these two companies on his present basis. You may wish to consider pressing him to bring forward more radical options which will bring the futures of Harlands and of Shorts to a head more rapidly.

2. You may wish to discuss the three companies in the order in which they appear in Mr King's paper.

i. Mackies. No immediate decisions are needed on Mackies. Mr King is satisfied that Howdens are financially sound and have the management resources to take over Mackies. He remains hopeful that Howdens will agree to rescue Mackies on reasonable terms. A Government dowry will be required, and the Treasury will have to approve the deal. You may wish to note the position but ask when he expects the deal finally to be concluded, perhaps with a view to inviting a progress report around the end of January if nothing is settled by then.

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ii. Harland and Wolff. Negotiations with Mr Tikkoo have collapsed and none of the other options for saving Harlands from closure looks particularly promising. Mr King wants to go on with the search for a possible purchaser and proposes to pursue a management/employee buy-out based on some tentative ferry orders from Sealink. He accepts that if his search is unsuccessful the Government will eventually have to consider the option of closure. For the short term you will wish to decide whether to approve an EFL of £62.3 million for Harlands for 1988-89. Looking ahead, you will want to judge when best to press for consideration of - and a decision on - closure. One possibility would be to ask Mr King to prepare for a meeting of E(A), perhaps around the end of January, a full assessment of the options for closure, with detailed costings and timetables. He will emphasise the enormous political difficulty of closure. But asking for this report would not prejudice the decision, only ensure that it was based on a properly informed view of the options.

iii. Shorts. Mr King is seeking offers for Shorts as a whole, not for individual parts. He indicates that the timetable for privatisation is likely to extend into 1989-90. In the meantime he proposes an interim reconstruction of Shorts' capital structure in this financial year, costing around £300 million, on the grounds that it will be needed whether or not the whole of Shorts can be privatised. We understand that Treasury Ministers want a fresh firm of accountants to review Shorts' books for a month, before any sales memorandum is issued, because of the company's worsening financial position. There is also some doubt whether the European Commission would approve a reconstruction in the absence of a clear plan for sale. You will wish to consider whether it is right to proceed with a capital reconstruction at this stage. One possibility would be to defer a decision until the end of January when the fresh accountants' report may be available and when the possibility of selling off parts of Shorts could be considered. You could also press Mr King to provide an estimate of the total cost of disposal, which he was asked for in October.

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BACKGROUND

3. On 6 October E(A) agreed that Mr King should continue to negotiate with potential private sector buyers of Mackies. On Harlands, E(A) recognised the difficult problems Mr King faced, but made clear that there had to be an end to the loss of public money at the yard, and that the current unsatisfactory position could not be allowed to drift. Mr King was also asked to ensure that documents on the AOR were released swiftly to Swan Hunters. On Shorts, E(A) endorsed the objective of privatisation by March 1989. They said it should be made clear to the management of Shorts that the Government was responsible for taking the lead in its sale. There was no question of Shorts developing new aircraft whilst it remained in public ownership, but the question of whether Shorts might be provided with launch aid once in the private sector was left open. Mr King was asked to set out Shorts' financial position, the anticipated cost of disposal, and details of Government guarantees for the company's finances in his report for this meeting.

ISSUES

MACKIES

4. There still appears to be a reasonable prospect that the Howden Group will be willing to purchase Mackies on reasonable terms. Mr King reports that Howden's financial position has been assessed following your comments at E(A) in October. He is satisfied that the Group is basically sound and has the necessary management resources to run Mackies. A dowry will be needed for the rescue to be agreed. Disposal of Mackies may now be possible in January, but this timetable may prove optimistic given past experience. We understand the Treasury expect the sale to proceed, although they think slightly more than the £20 million of assistance previously proposed may be needed to clinch the deal. Mr King has agreed to fund any assistance from within his block. Mr King is not asking for any decisions on Mackies at this meeting. You may wish simply to:

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- i obtain confirmation from Mr King that provision of a dowry would not be expected to cause problems with the European Commission;
- ii repeat that, as previously agreed, he will fund any assistance from within his block and clear the detailed support package with the Treasury when he is ready to finalise it;
- iii ask when he expects the deal to be concluded, perhaps inviting him to report progress at the end of January if it is not settled by then.

HARLAND AND WOLFF

5. Mr King's paper sets out the position on the three potential purchasers discussed in October: negotiations with Mr Tikkoo have ceased, Bulk Transport are resisting a takeover bid and talks with them have been adjourned, and doubts remain about the ability of the Turkish company UM Holdings to finance any takeover. Mr King suggests that a possible management/employee buy-out based on possible ferry orders from Sealink may be more promising, but this still sounds highly tentative. You may wish to ask Mr King for his honest assessment of the prospects of achieving a successful disposal of Harlands.

Performance Guarantee

6. Mr King says he has ruled out the possibility of offering a Government performance guarantee to potential purchasers of Harlands. Some potential buyers have said they would need such a guarantee to give comfort to their financial backers. You will want to confirm that a performance guarantee is not acceptable. You may also want to ask what Mr King has in mind in paragraph 8, in his statement that a management/employee buy-out could be restructured effectively to give such comfort to lenders, although without an explicit performance guarantee. The purpose of disposal must be to release the Government from continued responsibility for Harlands.

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EFL

7. Mr King seeks approval to setting an EFL for Harlands in the current year (1988-89) of £62.3 million. Some breakdown of this figure was included in his paper for the October meeting, but no decision was reached then. We understand the Treasury may be prepared to go along with this figure. You may wish to ask the Chancellor or the Exchequer whether he is content to endorse this EFL.

Options

8. If no credible buyer appears, the option of closure will have to be considered. You will want to judge when best to press Mr King to produce a paper on how closure might best be managed. If you felt that the position was already in danger of drifting, you could ask for a paper for a meeting at the end of January setting out options for closure, with the costs fully quantified and a clear timetable set. Mr King was asked at the meeting on 13 July to agree the cost of closing the yard with the Treasury, but has not yet done so.

9. There are two broad options for closure:

- i an orderly rundown, with clear dates set for the closure of particular yard facilities and numbers of redundancies. You will want to see this properly worked out and costed, with an assessment of how realistic it is to suppose that as the yard reduces in size work on the remaining orders will proceed normally. Mr King mentions (paragraph 10) the possibility of incentive arrangements or some form of management buyout to ensure that remaining work is completed, and you could ask him to explain what he has in mind in his further report;
- ii early complete closure, perhaps after work on SWOPS is completed in June 1989. Mr King may argue against even considering this course, given the political difficulties, and say that the AOR would never be completed. You may however want to postpone a decision until you see the costings of both

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options, and an assessment on how realistic the option of an orderly rundown is. You might also ask for an assessment of the option for dealing with AOR, for example transferring the work to Swan Hunter.

To maintain the momentum, you could ask for any reports to be completed in time for discussion in E(A) around the end of January.

Package of Remedial Measures

10. Mr King's paper suggests in paragraph 11 that, if Harlands were closed, a five-year package of remedial measures costing up to £90-100 million could be needed. Such cost would appear to be proportionately much higher than the package planned for Sunderland. At this stage you may simply wish to note that some remedial measures may be justified, but not give any commitment about the size of such a package.

SHORTS

11. Since the last discussion Mr King has continued trying to find a buyer for Shorts' entire business. We have heard informally that the Government's advisers on this sale, Kleinworts, think it unlikely that such a buyer can be found. This raises the question of how much longer Mr King should continue seeking a single buyer. You may wish to ask Mr King about the prospects of a single buyer being found on reasonable terms. Mr King will emphasise that he would face major political difficulties with the Shorts board and more widely in the Province if he proceeded to break up Shorts and to close parts of its business before every effort had been made to find a single buyer.

Financial Position

12. Mr King's paper describes in Annex 3 how Shorts' financial performance is worsening. In October the company's maximum in-year borrowings were predicted to be £131 million, during November. They are now expected to reach £146 million on 9 December. The company predicted an end-year EFL of £70 million in October, and predicts

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£98.6 million now; Mr King's officials think the actual figure could be £125 million. Mr King is not asking for an EFL to be set now. An EFL set more than half way through the financial year is obviously of limited value. You may however wish to confirm that the Chancellor is content not to set an EFL for this year.

13. We understand that Treasury officials believe it would be unwise for Mr King to send out a sales memorandum about the company on 16 December as he proposes (paragraph 16), until the Government has reconsidered its strategy. They are also dissatisfied with Deloitte's long accountants' report on Shorts, because they believe Deloitte has been primarily acting in the interests of the company's management. The Chancellor may therefore propose that a fresh firm of accountants be appointed to report within a month on the estimated cost of the complete sale, of options involving some disposals and some closures, and of complete closure. Their cover would be that they were preparing up-to-date figures on the company's deteriorating position. This would enable E(A) towards the end of January to decide, on the basis of proper figures, which option for Shorts should be pursued. The Chancellor might then want to be able to tell potential buyers, perhaps privately, that bids for individual parts of Shorts would also be considered. Although Mr King was asked on 6 October to include in his report for this meeting an estimate of the anticipated cost of disposal, no such estimate has been made available. Depending on the discussion, you may wish to endorse a Treasury proposal for a further report on the options for Shorts by the second half of January, in the light of full financial information on the cost of the various options.

Interim Reconstruction

14. Despite the lack of a buyer, Mr King proposes that there should be an interim reconstruction of Shorts' capital structure in this financial year, if possible, on the grounds that Shorts' past debts will need to be written off whether the business is sold or closed. A reconstruction would enable much of the cost of disposing of Shorts to fall in 1988-89, even if the final sale is no longer practical in this timescale. Mr King would want the sum involved - £300 million -

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to be a claim on the Reserve. We understand however that the European Commission may be extremely reluctant to approve a reconstruction in the absence of a clear plan for sale. You may wish to ask Mr King and the other Ministers concerned about the prospects for obtaining Commission agreement to an interim reconstruction. You may also wish to ask Treasury Ministers in particular if they are content for a reconstruction to take place before a further report by fresh accountants is carried out. Depending on the discussion, one possibility might be to defer a decision until the end of January when this further report is available and when the question of disposing of parts of Shorts could be decided.

HANDLING

15. You may wish to ask the Secretary of State for Northern Ireland to introduce the discussion on each company in turn. The Chancellor of the Exchequer and/or the Chief Secretary, Treasury will wish to respond first. The Minister of State for Defence Procurement may wish to comment on the implications for his Department of the prospects for Harland and Shorts. The Foreign and Commonwealth Secretary and the Trade and Industry Secretary may wish to comment on the handling of discussions with the European Commission on the provision of financial support for the three companies. Other Ministers may wish to contribute to the discussion.

R.T.W.

R T J WILSON
Cabinet Office
29 November 1988

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PRIME MINISTER29 NOVEMBER 1988NORTHERN IRELAND INDUSTRY

The NIO paper is disappointing in all three subjects. Progress on the sale of Mackies is slower than we were led to believe. The Harlands policy continues to be one of procrastination and pious hope while Shorts is being offered for sale on a basis designed to appease its chairman rather than to attract serious purchasers.

Mackies

For some reason which I have been unable to uncover, the Howdens team has taken fright at some item in the Mackies detailed accounts. This could well be an overvaluation of some asset or the imminent need for major capital expenditure to enhance assets. Alternatively, it may be an undisclosed liability or a contingent liability whose ultimate size is expected to be greater than that shown. Whatever it is, we are told that Howdens are still interested in the purchase but that they will need longer to evaluate its financial consequence.

The implications are therefore that Howdens will either pay less for the Mackies assets or expect a larger Government subsidy. I am told that the deal can still be struck with net Government funding of under £20 million. This was the figure mentioned at a previous E(A) when a solution based on quasi state ownership was proposed. You made two points at the time. First, that any resolution of Mackies should not leave the state as the true de facto owner; secondly, that any taxpayers' injection should be tranching, so that benefits from the initial investment should be evident before further money was committed. Both these principles

seem equally valid for the Howdens sale or indeed any other sale if that should disappear.

You should emphasise that (i) once Mackies is sold, it will have no special status where the Government acts as an ultimate financial safety net; and (ii) whatever capital injection is agreed should be tranched (unless this were all required at once which would be most unlikely).

Harlands

This is one of the highest cost and most incompetently run shipyards in the world. Its Chairman is an over optimistic salesman with limited imagination about financial consequences and even less appetite for financial responsibility. Last year's Deloitte report made that crystal clear. He misled the MoD about the true costs of AOR1, followed up but was rumbled on AOR2, and has completely misrepresented the commitment of Ravi Tikoo! The whole of E(A) knew that there was no substance behind Ravi Tikoo and we are now told that he is not prepared to invest a single penny of his own. Such would indeed have been 'the ultimate dream' if Government had fallen for it.

The NIO now wishes to go on pursuing further imaginary deals, including an MBO, for which the cash flow projections can only be ludicrous, in order to claim that HMG has 'pursued every possibility'. There is never a right time to close a shipyard and the temptations to procrastinate are legion as Tony Newton is discovering with NESL. The best time to make a closure decision is when a yard has plenty of work so that employment effects can be anticipated and thought through.

The hard prospect of closure may incline the workforce to reduce existing work to a snail's pace but this can be counteracted by incentive payments linked to deadlines.

Such additional costs are part of the overall closure decision and should be so treated. It is no solution to enter a vicious circle of procrastination so that the yard actually runs out of work before a decision is made. That is high level incompetence and would leave a longer and blacker political mark than planned closure with adequate planning.

If Tom King presses he should be given a short period, measured in weeks rather than months, to pursue and finalise a privatisation scheme. This indicates a decision point in mid-January which would avoid political allegations of heartlessness over Christmas.

Shorts

Kleinworts, acting for the Government, have been instructed to promote the sale of the business as a single entity. This would be marvellous but it is naive to propose it as the only basis for privatisation. My previous paper (attached as Annex) presented the commercially viable missiles activity as a separate free standing business employing 1500 people and worth approximately £70 million. The good is often driven out by the bad and it is wrong to tie the future of this potential success inextricably to the fortunes of the aircraft business.

Tom King has rejected launch aid for the FJX but is nonetheless asking for a £300 million capital injection this financial year, in advance of any sale having been resolved. Putting myopic considerations first, the Treasury may well support him. My fear is that a substantial financial settlement, in advance of any prospect of sale or even of any realistic proposal for selling, will simply disappear. By the time a viable deal is resolved, which will probably include part sales and part closure, the £300 million will simply have gone into the general morass. Recall, that the

present Chief Executive, McNulty, was in charge of finance when the Shorts external financing requirement so overshot its budgetted EFL that its magnitude was for months a matter of speculation! It would therefore be appropriate to ask what is the overall figure which NIO current believe to be covered by Government assurances. For all their faults, at least Rover knew the size of their current and projected VJM assurances!

The Treasury wish to put £300 million into this year's public expenditure in the belief that next years requirement will be £300 million less! My advice is that no new Government money should be put into Shorts until a viable sales plan has been established. Its commercial borrowings will move in line with business requirements which must be considered when setting its EFL. However that is far different from simply handing over £300 million for a 'restructuring exercise'.

The Treasury will seek to advance the £300 million on the strict understanding that the business is offered for sale in a more realistic form, namely with its separate components evaluated independently. It will also argue that external borrowings should be cut to, say, £50 million. With the financial incompetence at Shorts so recently exposed, the cavalier and arrogant contempt for his shareholder which the Chairman has so recently demonstrated, and with the NIO's evident inability to control its nationalised industry, any such settlement would be a mistake.



GEORGE R GUISE

PRIME MINISTER5 OCTOBER 1988MACKIES/HARLANDS/SHORTSMackies

It is good to hear that there is one potential buyer showing some enthusiasm. Any viable deal will probably require Government funding which can only be justified on political grounds. Furthermore it is essential that it is a genuinely private solution which emerges. One earlier proposal placed a commercial bank in the false position of appearing to finance Mackies while its risks were totally underwritten by government. This is merely disguised nationalisation and Tom King should be disabused that any final solution of that kind will be acceptable.

The original Government investment mentioned was £20 million in order to render the business 'commercially viable'. Your own proposal was to tranche any Government investment so that the benefits of the initial amount would have to become evident before anything further was ventured. It might be appropriate to remind Tom King of that in any encouraging remarks that are made. Nevertheless Mackies appears to be the brightest spot in a very gloomy picture.

Harlands

It is no surprise that the Tikkoo deal is proving hollow. It was most improbable that Tikkoo could make economic good out of Harlands without enormous Government subsidies. His background gives no indication that he could become a chief executive capable of giving Harlands hope of real economic viability. Further dealings with Tikkoo seem both a waste of time and a diversion of effort. It is unlikely that he

can raise private financial backing of the scale required. The Northern Ireland Office should now press on with those other possibilities which the paper mentions under a strict time limit of about two months to produce something viable.

Tom King should be warned against a hastily cobbled deal which technically privatises Harlands without solving any of the yard's underlying problems. This will only rebound on the Government, probably at an awkward time. Far better to face up to closure of Harlands in a planned manner if a genuine sale cannot be achieved in the immediate future. As an interim measure I understand the Treasury will not object to the proposed EFL of £62.3 million.

Shorts

The NIO paper glosses over a major row which Tom King and Paul Viggers have been having with the Shorts Chairman, Rodney Lund. Lund is totally opposed to piecemeal privatisation despite the fact that the only part of the business which has attracted any interest is the missile division. When the Government's intention to sell Shorts was announced in July, Lund accused Viggers of giving a 'totally misleading government briefing' in which management was openly criticised. There was a subsequent vitriolic exchange when Lund even threatened to sue for defamatory statements. - see Annexure A from Lund to King dated 20 July.

Lund further argues that any proposal to sell the missiles division separately (valuations indicate an order of £70 million) will lead to an immediate sit-in by unions at the Aircraft and Aerostructure plant leading to massive liabilities for non-delivery to Boeing. Lund claims that Government has an obligation to meet Shorts' debts because of an assurance given in Parliament by a previous Northern Ireland Secretary of State (cf - the Varley-Marshall

assurances for Rover.) He suggests that the downside risk to Government in pursuing a separate sale of the missile division could therefore be over a billion pounds! The Treasury are highly sceptical about this.

There is no commercial logic in binding the successful missile business, which is physically separate from Shorts main factory with no commonality of manufacture or cross costing benefits, to the heavily loss making aircraft and aerostructure business. The missile division has a turnover of £80 million and 1,500 employees. Its performance is variable but it is basically profitable and has been valued at £70 million. With the Starstreak missile under development, it has a secure medium term future.

By contrast the aircraft (turnover £90 million) and aerostructure (turnover £70 million) activities operate from a single site employing 6,200 people and sharing common resources and facilities. This business is unprofitable and poorly equipped. Shorts management argue that it can only become viable after developing a new short range aircraft - the FJX. This would be a twin jet capable of transporting 44 passengers up to 1,760 kilometres.

Gross investment for this project has been estimated at £500 million of which Shorts would carry £180 million after allowing for investment by partners and sub-contractors. Shorts would want half to be financed by Government launch aid as well as immediate debt restructuring of £300 million for the company overall. This constitutes the nearly £400 million Government investment mentioned in the last E(A) paper which King did not support. Such an amount is of the same order as closure costs and would be in total contravention of Brussels' position on State aid. It is the old Rover argument. Give us the capital for new models and we will set the business right.

You may not wish to bring all this out at E(A) but it is important to be aware of the atmosphere in which King has delegated the privatisation of Shorts to its Chairman and Board as set out in Paragraph 11 of the NIO paper.

Conclusion and Recommendation on Shorts

There has been a very bad relationship between the Shorts Chairman and Northern Ireland Ministers. Instead of firing Lund, Tom King has handed him the business to sell. This is a very high risk strategy, particularly as Shorts is the largest employer in Northern Ireland.

In strict commercial terms the obvious solution is to sell the missile business to a company like Ferranti who have shown interest. Sale of the aerostructures business should also be attempted, perhaps to a consortium of its customers. However, the aircraft business is not viable without a massive Government dowry and the commercial solution must be closure.

It may be that we have no alternative but to stay with Lund for the immediate future, because there may be no one better to take the job. However you should test this assumption very carefully, either with Tom King privately or, if appropriate, during E(A). In my experience, whenever the shareholder abandons its business to a potentially hostile management, no good results. It would be far better if responsibility for privatising the company could be separated from its present management.



GEORGE GUISE

SECRET

ANNEX A

SHORTS

Rodney Lund

RL/CMH

July 20, 1988

The Rt. Hon. Tom King MP
Secretary of State for
Northern Ireland
Northern Ireland Office
Old Admiralty Building
Whitehall
LONDON SW1A 2AZ

Dear Secretary of State,

I hardly have to tell you how utterly dismayed I am about the recent leakages to the Press of information confidential to this Company and to read the quite extraordinary and defamatory statements about the Management. A reasonable man might wonder if there was some wish to sabotage the Company.

I think you will agree that the damage to the Company is so serious that I have no option but to write to the Prime Minister for help which I have done today.

Most damaging of all to the Company are the press statements that we have lost £85m in the first quarter. Suddenly the most horrendous thought crosses my mind. Can it be that you have been wrongly briefed? The pre-interest loss for Shorts for the first quarter is in fact some £10m - and this is traditionally our worst quarter. The £85m is simply a measure of our peak cashflow operational requirement and is not unusual for this time of the year.

When we last met I could not understand your remarks about massive haemorrhaging because I knew our quarterly results would not be too far off target. Is it possible that you really thought we had lost £85m? Certainly whoever leaked this confidential figure to the Press must have thought so. It would scare me too much if I thought that recent decisions about the Company might have been predicated by someone in the system who did not know the difference between profit and cashflow.

I enclose a copy of a letter from our lawyers to Mr. Viggers which is self explanatory.

*Yours sincerely
Rodney Lund*



dti

the department for Enterprise

CCPV

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The Rt. Hon. Tony Newton OBE, MP
Chancellor of the Duchy of Lancaster and
Minister of Trade and Industry

Rt Hon John Major MP
Chief Secretary
HM Treasury
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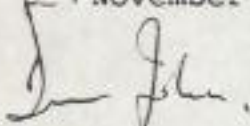
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29 November 1988



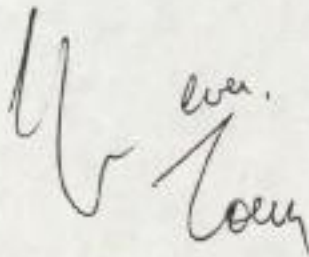
BRITISH SHIPBUILDERS AND THE NORTH EAST

Thank you for your letters of 26 October ^{flag} and 7 ^{flag} November. As you will have realised, your 26 October letter effectively crossed with mine of 31 October to Malcolm Rifkind.

On the 26 October letter, I am afraid we shall have to accept that a Sunderland company would be funded through British Shipbuilders. We have not been able to discover any alternative suitable powers. However, I do intend that the new company, should it be needed, will be identified as closely as possible with Sunderland and not with British Shipbuilders. I shall also seek to ensure that financial control is no less effective than that exercised directly by my Department.

On the question of who should pay for site clearance, I take the point in your letter of 7 November. My officials understand from British Shipbuilders that site clearance of previous shipyards generally pays for itself because of the high scrap value of metal clad buildings and metal fittings. For this reason it is unlikely to be the Corporation's commercial disadvantage to arrange the job themselves.

I am copying this letter to the Prime Minister, Members of E(UP), Paul Channon and Sir Robin Butler.



TONY NEWTON

EM3ACD

NAT IND: Shipbuilding
Pt 15 ●



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Papers removed from file

Date 29.11.88

CDL to CST 29.11.88

NAT IND: Skipton, 10/11/85
Pt 15

British Shipbuilders

3.30 pm

The Chancellor of the Duchy of Lancaster and Minister of Trade and Industry (Mr. Tony Newton): With permission, Mr. Speaker, I wish to make a statement on progress in returning British Shipbuilders to the private sector, in accordance with the policy described to the House by my predecessor on 18 April and 21 July. I felt that the House would rightly wish to have such a report before the forthcoming parliamentary break. I should, however, make it clear at the outset that I am not yet in a position to resolve all the remaining uncertainties.

When my predecessor made his statement in April, British Shipbuilders owned shipyards at Govan, Sunderland, Appledore and Port Glasgow, together with the Clark Kincaid marine engine builders on the Clyde and a services subsidiary, Marine Design Consultants, at Sunderland and Dundee. Together these accounted for some 6,500 employees—less than 20 per cent. of total United Kingdom employment in shipbuilding, which is of the order of 35,000.

The Govan shipyard was successfully sold in August to the Norwegian Group Kvaerner Industrier. It has made a major inward investment in Govan, which is now to be the centre of its advanced gas ship technology. Kvaerner has so far placed orders for two gas-carrying ships at Govan with the possibility of similar orders to follow. The future of the yard now seems assured. Negotiations for the sale of Clark Kincaid to a management buy-out team have gone well. They have been materially helped by Kvaerner's confirmation, at the time of my visit to it, in Oslo two weeks ago, that the engines for the first two gas-carrying ships to be built at Govan would be built at Clark Kincaid. I am glad to say that all commercial matters have now been agreed. I hope that the sale will be successfully completed by the end of the year.

Negotiations have also been proceeding for the sale of the Appledore yard to Langham Industries. Langham hopes to place significant work with the yard, with continuing Government support under the intervention fund. The House will be pleased to know that Langham Industries and British Shipbuilders are now close to agreement. Again, I hope that this sale will be completed by the end of the year.

In the case of the Ferguson yard at Port Glasgow, I can also report further progress. British Shipbuilders has today named a preferred bidder. This is Ailsa Perth Ltd., which previously bought the Ailsa yard at Troon. Detailed negotiations will now get under way, and I have, of course, asked British Shipbuilders chairman, John Lister, to ensure that every effort is made to bring them to an early and satisfactory conclusion. I can also tell the House that bids have been received by British Shipbuilders for Marine Design Consultants. These are currently being evaluated by British Shipbuilders and its financial advisers.

The yards and other facilities to which I have so far referred account for nearly two thirds of those employed by British Shipbuilders at the start of this process. The other major element of British Shipbuilders is North East Shipbuilders Ltd. at Sunderland. This consists of building yards on either side of the Wear, at Pallion and Southwick, together with Sunderland Forge Services and a fitting-out yard at North Sands.

As the House knows, British Shipbuilders asked for bids for NESL by 30 September. Four bids were received. At a late stage in their evaluation during October, one of the bidders sought to modify his offer. As I told the House on 26 October, I therefore thought it right to allow a further short period for all those who had submitted bids to modify them if they wished before a final assessment was made. Subsequently, we have also given time for further talks related to the possibility of a Cuban order for cargo ships, and to seek clarification of a tentative indication of a new overseas interest.

I will deal first with the original bids, as modified. I have to tell the House that, following consideration by British Shipbuilders and its financial advisers, the chairman has told me, and I have accepted, that none of them is acceptable.

None of those bids had the combination of shipbuilding experience and solid financial backing which, in the Government's view, would be required to sustain a viable operation in the extremely difficult conditions of the world shipbuilding market. Each also raises specific difficulties. One of them was in practice not a detailed bid, and depended on the granting of a licence for dumping waste at sea which itself would take some considerable time to resolve. Another offered continuing employment for less than a tenth of the work force. The other two, which would themselves have entailed major redundancies, required a degree of subsidy which would have been highly unlikely to be permitted under the sixth directive. One of the last two was in fact last week withdrawn.

I can, however, tell the House that during the past few days British Shipbuilders has received three clear expressions of interest in a possible purchase of facilities at Sunderland, including the overseas concern to which I referred earlier. In these circumstances, I have agreed with the chairman of British Shipbuilders that an opportunity should be allowed to consider proposals from these interests. This will also enable those making them, if they wish, to be fully informed of the outcome of the talks which have been taking place between the Cuban shipping company Mambisa and its financial advisers in London, whose representative is due to return to this country tonight.

We want to establish, by the end of this month, whether proposals can be developed which give a firm basis for negotiation. That would entail a clear statement of the work envisaged for the yard, evidence of the technical and financial capacity of the bidder, and the prospect of arrangements likely to be compatible with the European Community sixth directive concerning state support for shipbuilding.

These are not easy criteria to satisfy, as we have seen in assessing the earlier bids. No one should underestimate the difficulties. Nevertheless, I am convinced that it is right to make this last effort to find a viable way forward for NESL on the basis that I have described, and I believe that the House will share that view.

Mr. Bryan Gould (Dagenham): Is the Minister aware that there will be great relief at this further stay of execution for NESL, but that there will be an equally heartfelt hope that he recognises at last that merchant shipbuilding matters too much to Wearside and the British economy to be sacrificed on the altar of privatisation? Will he join me in paying tribute to the "save our shipyard"

[Mr. Bryan Gould]

campaign, the work force and the local community and its elected representatives who fought so hard to keep those yards open?

Will the Minister now say that his first priority is to secure the orders, especially the Cuban order, which will guarantee the future of these yards, and that this urgent and practical necessity will take priority over questions of ownership? In particular, will he guarantee that contracts will, if offered by the Cubans, be signed by North East Shipbuilders Ltd., irrespective of who is the owner for the time being?

Will the Minister concede that what matters to Sunderland and the British economy is to keep British merchant shipbuilding alive, and that the dogma of privatisation must now take second place? Will he recognise that we must now hope for more than the prolonging of a quite unnecessary agony of the Government's own creation and that he must now summon the courage to fight his corner with the EEC, to override his civil servants and to depart from the course mapped out by his predecessors and by the Secretary of State? Will the Minister now concentrate instead on building a viable future for shipbuilding on the Wear so that it can take advantage of the upturn in world demand for shipping and continue to make a vital contribution to our industrial future?

Mr. Newton: Far from the yards being sacrificed on the altar of privatisation, as the hon. Gentleman put it, the problem that we face is to rescue them from the disaster that nationalisation has been for them. It has led to British Shipbuilders costing the taxpayer overall about £2 billion since 1979, and on shipbuilding contracts alone it has lost £650 million, of which only £250 million has been within the permitted subsidy limits allowed by the agreed arrangements within the Community.

The hon. Gentleman referred to the possible Cuban order. No one should underestimate the difficulties of securing such an order against the intense competition that exists. However, in the circumstances that I described in my statement, in which further talks have been taking place in Cuba this week, I have felt it right to allow time for the outcome of those talks to be properly assessed. I cannot hold out hope, against the background of what I have already said about the losses made by British Shipbuilders, which include large losses made by North-East Shipbuilders, of British Shipbuilders taking the contract, as the hon. Gentleman asked.

The hon. Gentleman also made remarks about my colleagues and my civil servants. In the past few weeks, I have given clear evidence to him and to the House that my purpose is to find a way of permitting the viable continuation of shipbuilding on Wearside, if that can be achieved. The hon. Gentleman should in turn recognise that the difficulties are great and that the optimism that has been expressed about an upturn in world shipbuilding orders, which I have read about, has to be judged against the fact that within the past few weeks the Association of West European Shipbuilders has drastically revised downwards its forecast of the upturn from annual orders of nearly 19 million compensated gross tonnes in the half decade from 1990 to 1995 to about 12.5 million compensated gross tonnes. What the hon. Gentleman has said needs to be judged against that.

Miss Emma Nicholson (Totridge and Devon, West): Is my right hon. Friend aware of the constructive way in which the work force at Appledore has tackled privatisation and of its genuine gratitude to my right hon. Friend and the chairman of British Shipbuilders for the time they took to listen to the work force's views?

Mr. Newton: I am grateful to my hon. Friend for her comments and also for the constructive part that she has played in developing the arrangements. As I said in my statement, I am now hopeful that they will lead to a secure future for her constituents who work at Appledore, about whom she is rightly concerned.

Mr. Ernie Ross (Dundee, West): Does the Minister accept that there will be great fear in Scotland about whether the Ferguson yard will continue to operate? Will the Minister give assurances that the unions at Ferguson will have an opportunity to make an input into deciding on the preferred buyers? Will he also confirm that Marine Design Consultants of Dundee has put in a bid, and that it has been accepted? Will the Minister ensure that its bid is given an equal opportunity, against the voiced intention of the present managing director, who has made it clear that if he is allowed to buy both yards it is likely that he will want to close one of them?

Mr. Newton: British Shipbuilders today named a preferred bidder for Ferguson. It will be up to the preferred bidder to decide whether to hold talks with the work force and I expect that a preferred bidder would want to do that. We should not want to place any obstacle in the way. The hon. Gentleman asked me about Marine Design Consultants. I cannot add to what I said in my statement. Bids have been received and are being evaluated, and it would be wrong of me to comment further until I have received advice from British Shipbuilders. When I have, I shall take account of the hon. Gentleman's point.

Mr. Barry Field (Isle of Wight): Can my right hon. Friend comment on the disputed ferry contract? Does he realise that his decision to limit the period to the end of the month will be widely accepted, not only by the work force but by the industry generally, as it will clear up the uncertainty hanging over the yard?

Mr. Newton: I thank my hon. Friend for the latter part of his remarks. The collapse of the Danish ferry order has been one of the factors that have aggravated NESL's problems in recent weeks. Of the original 24 ferries ordered, 15 are being built and nine are not. Two of the ferries have been delivered, 10 have been completed and three are yet to be finished. Some will require further modification. Negotiations are taking place in the wake of the cancellation of the contract but they have not yet been completed.

Mr. James Molyneux (Lagan Valley): Having visited the north-east only two weeks ago, may I ask the Minister whether the implications of the EEC Sixth directive and its effects on British Shipbuilders and Harland and Wolff were fully understood when the Government embarked upon the policy of privatisation?

Mr. Newton: I do not think that there has been any mystery in the industry about the general requirements and conditions of the Sixth directive, under which intervention fund payments are made in appropriate

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10 DOWNING STREET

LONDON SW1A 2AA

From the Private Secretary

14 November 1988

Dear Peter,

BRITISH SHIPBUILDERS

The Prime Minister has seen the Chancellor of the Duchy of Lancaster's letter of 11 November to the Chief Secretary. She is content with the terms of the proposed statement to be made today, but has commented that she hopes it will be possible now quickly to bring matters to a conclusion at NESL.

I am copying this letter to Clive Norris (Department of Employment), David Crawley (Scottish Office), Mike Maxwell (Northern Ireland Office), Roger Bright (Department of the Environment), Alison Smith (Lord President's Office) and Trevor Woolley (Cabinet Office).

*Yan,
P.G.*
PAUL GRAY

Peter Smith, Esq.,
Chancellor of the Duchy of Lancaster

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FILE SLH
cc BG.

KK

The Rt. Hon. Tony Newton OBE, MP
Chancellor of the Duchy of Lancaster and
Minister of Trade and Industry

Rt Hon John Major MP
Chief Secretary
HM Treasury
Parliament Street
LONDON
SW1P 3AQ

Department of
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Telex 9811074/5 DTHQ G
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Prime Minister

*The NESL saga is
dropping or renouncingly -
it would have been better to
bite the bullet earlier. Re,
staying for here, Mr. Newton does make a
reasonable case for this proposed future
interim statement on Monday. Contact to
agree the statement, while ~~is~~ urging Mr.
Newton now to bring matters quickly to a
conclusion?*

Direct line
Our ref
Your ref
Date

215 5147

11 November 1988

Dear Chief Secretary,

REC6
"1" Yes not

BRITISH SHIPBUILDERS

My letter of 3 November reported two significant developments on the future of North East Shipbuilders Limited: interest by a Japanese group in acquiring the yard; and attempts by Lloyds Bank to restructure a consortium bid, possibly including a Tate and Lyle interest, and centred on a potential order from Cuba. At my request, John Lister has been urgently pursuing both of these developments in the course of this week.

Tate and Lyle proved not to have any interest in joining a consortium or in becoming involved in any other way with NESL. Lloyds Bank have been holding further talks in Havana on the possible Cuban order. I have ensured that our Embassy represented us at these talks which will not be completed until next Monday. No further information has emerged on the price they would be prepared to pay but both John Lister and I are sceptical that there is any price which BS could meet. The Cubans have indicated they are flexible on delivery dates and are prepared to move quickly to secure a deal this year. On the other hand it is highly implausible that firm contracts with a new owner for the yard could now be signed by the end of the

year when there is a strong likelihood that the level of Intervention Fund support permitted under the Sixth Directive will be reduced from the present 28% to, say, 23%. This would of course make it even less likely that a UK yard could take the order.

I have to conclude, in the light of these developments, that there is a risk that the Cubans are "playing politics" and will do what they can to make it difficult for me to take a final decision. In the meantime, however, there is a difficult presentational point. The Lloyds Bank representative will not be returning from Havana until Tuesday 15 November. I fully expect that, whatever I try to say in a Statement before then, they will seek to contradict on the basis of their detailed information from the talks. This points towards not taking a final decision at this stage.

The strength of the Japanese interest is also unclear. John Lister has been doing his best to get a feel for how committed they might be. He has now written to me saying that his representative in Tokyo has reported to him that the company remains very interested in pursuing a way of taking a major interest in NESL and is hopeful that we will have a formal letter from the President by Monday 14 November confirming this. John Lister's own view is that the Japanese are more than interested but, unless and until a letter is received, he cannot be more precise.

In the light of these developments, I have been considering the Statement I should make to the House on 14 November. I am in no doubt that I have to make a Statement that day. There has been considerable speculation about what has happened to the bids that have so far been submitted and I have previously undertaken to keep the House informed. With prorogation imminent, I feel I have to report the position. Moreover, there is very good news to report on progress with disposals of the other remaining BS facilities.

I have previously stated that I am concerned to ensure that every avenue for selling NESL has been fully explored. I think it would be indefensible, particularly in the light of John Lister's letter to me, not to establish how interested they were before taking a final decision. As I said in my previous letter, if the Japanese interest does prove to be serious then sale to them could well cost less than the total cost to the Exchequer of closure of NESL. As I have also mentioned, there is a difficult presentational point with respect to the position on Cuba. I have therefore decided that my Statement on 14 November should leave open the Japanese option. I shall not be announcing closure.

I attach a copy of my draft Statement on which I would welcome your comments. As you will see, despite the interest that has so far been shown, my assessment is that there can now be little doubt that at least some of the NESL facilities will close. I have also restated my commitment to BS not being allowed to take the Cuban order whilst NESL remains in public ownership.

I should also mention that my Department was today approached by Mr Ian Sproat asking whether we would consider a bid from "a UK blue-chip company" for NESL. He has since been trying to contact John Lister. Without knowing a lot more of the detail, I am rather sceptical that this will amount to a firm proposal but, while discussions are continuing with the Japanese, I do not think it would be right to rule it out. I do not of course wish to refer to this approach in the Statement. It is therefore drafted in terms of my having agreed that John Lister could consider any new bids from other sources. I have made clear to John Lister, however, that I certainly do not see this as the start of another lengthy bidding process and that he needs to establish, as quickly as possible, whether he can move to a preferred bidder stage with any of the current interests, including the Japanese.

I am copying this letter to the Prime Minister, Norman Fowler, Malcolm Rifkind, Tom King, Nicholas Ridley and John Wakeham and to Sir Robin Butler.

Yours sincerely,

Peter Smith

TT TONY NEWTON

*(Approved by the Chancellor
and signed in his absence)*

DRAFT STATEMENT ON BRITISH SHIPBUILDERS

With permission, Mr Speaker, I wish to make a statement on progress in returning British Shipbuilders to the private sector.

The Government's policy was set out clearly by my predecessor, my Rt Hon and Learned Friend the Member for Rushcliffe, in his statement to the House on 18 April. British Shipbuilders has cost the taxpayer some £2bn since 1979. In respect of shipbuilding contracts alone, losses amount to approximately £750m, of which only £250m represents Intervention Fund subsidy within the agreed European Community limits.

The Government can see no justification for the taxpayer to continue to bear such losses, nor any prospect of British Shipbuilders in its existing form being able to restore the yards to viability. We therefore decided to seek private sector purchasers for the yards, with any future Government subsidy limited to that provided by the Intervention Fund, currently a maximum of 28% of the cost of a ship.

When my predecessor made his statement, British Shipbuilders owned shipyards at Govan, Sunderland, Appledore and Port Glasgow, together with the Clark Kincaid marine engine

builders on the Clyde and a services subsidiary, Marine Design Consultants at Sunderland and Dundee. Together these accounted for 6,500 employees - less than 20% of total UK employment in shipbuilding, which is of the order of 35,000.

The Govan shipyard was successfully sold in August to the Norwegian group Kvaerner Industrier, which placed orders for two gas-carrying ships with the possibility of similar orders to follow.

I am pleased to announce that negotiations for the sale of Clark Kincaid to a management buy-out team has reached the stage of a Letter of Intent. This has been helped considerably by Kvaerner's confirmation, following my visit to them in Oslo two weeks ago, that they would purchase from the firm the engines for the first two gas-carrying ships to be built at Govan. I have every hope that Clark Kincaid will be successfully sold by the end of the year.

Members will also be aware that negotiations have been proceeding for the sale of Appledore to Langham Industries. Here again I am delighted to announce that Heads of Agreement have been signed today. Langham hope to place significant work with the yard, with continuing Government support under the Intervention Fund, and the long term future of the yard seems assured. I expect the sale to be completed shortly.

In the case of the Ferguson yard at Port Glasgow, I am again pleased to announce that British Shipbuilders now have a preferred bidder. The firm is Ailsa Perth Limited, who previously bought the Ailsa yard at Troon. I have asked the British Shipbuilders Chairman, John Lister, to bring these negotiations to an early, and hope satisfactory, conclusion.

Finally, I am pleased to report that four bids have been received by British Shipbuilders for Marine Design Consultants. These are currently being evaluated by BS and their financial advisers.

Mr Speaker, I turn now to the largest remaining element of British Shipbuilders: North East Shipbuilders Limited at Sunderland, consisting of building yards on either side of the Wear at Pallion and Southwick, together with Sunderland Forge Services and a fitting-out yard at North Sands.

As the House knows, BS asked for bids for NESL by 30 September. Four bids were received. These were being evaluated when, as I told the House on 26 October, one of the bidders sought at a very late stage to modify his offer. I therefore thought it right to allow a further short period for all those who had submitted bids to modify them if they wished before a final assessment was made. Subsequently, we have also given time for further talks which could affect the possibility of an order for cargo ships for Cuba, and to

clarify whether there was any real substance in a tentative indication of a new overseas interest in purchasing some or all of the Sunderland facilities.

The four original bids were carefully considered by BS and their financial advisers. I am disappointed to have to tell the House that the Chairman has recommended to me that, on financial and commercial grounds, none of them is acceptable. I have accepted this recommendation.

None of the bids has the combination of shipbuilding experience and solid financial backing which, in the Government's view, would be required to sustain a viable operation in the highly uncertain conditions of the world shipbuilding market. Each of the bids also raises specific difficulties. One of them was in practice no more than a proposal and depended on the granting of a licence for dumping waste at sea which itself would take some considerable time to resolve. Another involved making the entire workforce redundant offering only piecemeal employment thereafter. The other two, which would themselves have entailed major redundancies, required a degree of subsidy which would be highly unlikely to be permitted under the Sixth Directive.

As regards the possible order for cargo ships for Cuba, my Department was recently advised that the Cubans were looking for a tender of less than £10m per ship and that the Cubans

hoped to place an order in the very near future. Further talks took place in Havana last week at which the Government was represented. At the conclusion of those talks, there was no firm indication of any change in the Cuban position on price. As regards the timescale, the Cubans appear not to be in any hurry to place the order and may well be prepared not to do so until sometime next year.

The British Shipbuilders Chairman has advised me that, even with Intervention Fund support, the lowest price at which he would have been able to tender would have been £15m per ship, more than 50% above what the Cubans had at one stage said was their indicative price. Moreover, in the absence of any firm indication about timing, it is extremely difficult to decide how seriously the bid should be taken. I therefore have to tell the House that, as my predecessor made clear, there can be no question of British Shipbuilders taking the order and I very much doubt that any private sector purchaser would be able to do so. Indeed, one of the original four bidders for NESL has announced that he no longer wishes to be considered because he could not possibly have taken the order at this price.

This is not say that we have reached the end of the process of seeking private sector purchasers for NESL. I am able to report that British Shipbuilders have received a firm expression of interest from a major overseas industrial concern with which they have been in contact over the last

few weeks. In view of this interest, I have decided that a further period should be allowed for confidential talks to continue. I shall of course keep the House informed of progress.

While these talks are continuing, I have agreed with John Lister that he should be prepared to consider any new bids that may come forward. In leaving the door open in this way, however, I have to make clear that the view of British Shipbuilders and the Government is that it is unlikely that any successful bidder for NESL would want to keep all of the existing facilities open. This reflects the continuing strongly competitive world shipbuilding market. This is confirmed in the latest assessment by the Association of West European Shipbuilders which has revised downwards its forecast for orders in the period 1990-95 from £19m to £12.5m Compensated Gross Tonnes per year, a reduction of one third.

Mr Speaker, I regret that I am not able to give the House a definitive answer on the future position of NESL. I appreciate the concern over the continuing uncertainty, particularly on the part of those whose livelihood depends on the yards. I am sure, however, that Members will agree with me that, while there is still some hope of securing a viable long term future for the yards, we must ensure that every avenue is fully explored.

NAT Ind. Shipbuilding
Pt 15





SCOTTISH OFFICE
WHITEHALL, LONDON SW1A 2AU

cc P/A

The Rt Hon Tony Newton OBE MP
Chancellor of the Duchy of Lancaster
and Minister of Trade & Industry
Department of Trade & Industry
1-19 Victoria Street
LONDON
SW1H 0ET

NBN

Per

10/11

10 November 1988

Dear Tony,

Har

Thank you for your letter of 31 October.

I am glad that you are confident you will be able to meet my concerns, and, like you, I hope the issue will not arise. I should perhaps clarify the point that I am already supporting through my own programmes a wide range of remedial measures in areas where British Shipbuilders have had a presence. The particular point that I was concerned about in my letter of 18 October was the likely reaction in Scotland to new measures made available exclusively to redundant British Shipbuilders' employees in Sunderland through British Shipbuilders. If you choose this route my feeling is still that there may be pressure, through British Shipbuilders and their former employees in Scotland, for equivalent measures to be made available, in addition to the remedial measures not specific to British Shipbuilders which I am already supporting through my programmes. If there is such concern, all I would be able to do would be to refer representations to you, making clear that I have no Ministerial responsibilities for British Shipbuilders.

Copies of this letter go to the Prime Minister and members of E(UP) and to Sir Robin Butler.

Yours ever,
Malcolm Rifkind

MALCOLM RIFKIND

NAT 1NO: Shipbuilding PMS

cc: [unclear]



Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon Tony Newton OBE MP
Chancellor of the Duchy of Lancaster and
Minister of Trade and Industry
Department of Trade and Industry
1 - 19 Victoria Street
London
SW1H 0ET

NBM
RC6
SL

7th November 1988

Dear Tony,

BRITISH SHIPBUILDERS AND THE NORTH EAST

I have seen a copy of your letter of 31 October to Nick Ridley.

I see no difficulty with British Shipbuilders co-operating in the clearance of the shipyard sites at Sunderland on the basis that the site clearance is to BS's commercial advantage in disposing of the yards, and that the costs of clearance are recovered in higher sale proceeds. If clearance cannot be done on this commercial basis, I would expect such costs to be met within your and Nick's existing provision, as I have already made clear in respect of any UDC costs within Nick's urban expenditure.

I am copying this letter to the Prime Minister, members of E(UP), Paul Channon and Sir Robin Butler.

Your Ever, *John*
JOHN MAJOR

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Shipbuilding pt 15

dti

the department for Enterprise

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7/11

The Rt. Hon. Tony Newton OBE, MP
Chancellor of the Duchy of Lancaster and
Minister of Trade and Industry

Rt Hon John Major MP
Chief Secretary
HM Treasury
Parliament Street
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RHC 2

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RHC
4/11

Direct line 215 5147

Our ref

Your ref

Date

3 November 1988

mt

Dear Chief Secretary,

BRITISH SHIPBUILDERS: NORTH EAST SHIPBUILDERS LTD

I promised the House on 26 October that every avenue would be explored before a decision on the future of North East Shipbuilders is made. There have been two further developments.

First, in the wake of unfruitful discussions in August between BS and two Japanese shipbuilders about NESL, a third has made contact with BS representatives in Japan. This yard is not part of an industrial group like its predecessors, but is privately owned by a major businessman who is to see BS representatives later this week. His shipbuilding people are said to be keen on making a bid.

While it would be very difficult to make a Statement announcing the closure of the yards in advance of such a meeting, I shall require very clear evidence of serious interest to delay matters further. On the other hand, if the interest proves serious, it could well cost less than the total cost to the Exchequer of closure.

OC5ABK



the department for Enterprise

Second, although none of the original bids is satisfactory, Lloyds Bank is seeking to restructure the consortium they have supported with their Cuban interests in mind. They have already sought to involve Tate & Lyle, which has existing interests in shipbuilding and in Cuba. Again I shall not give credence to their efforts unless powerful evidence is forthcoming quickly that leads John Lister to believe he could make a positive recommendation about the consortium.

In view of these developments, I concluded that I could not make an announcement today as I had previously intended. I attach a copy of the on the record briefing used by the DTI press office today. I will keep you closely in touch with developments. I expect to write again early next week.

I am sending copies of this letter to the Prime Minister, with whom I discussed the position in the House on Tuesday night, John Wakeham and to Sir Robin Butler.

Yours sincerely,

Peter Smith

PP TONY NEWTON

(Approved by the Chancellor
and signed in his absence)

BRITISH SHIPBUILDERS

On the record briefing by DTI, 3 November

The evaluation of the bids, including in some cases revisions made late last week, has not yet been completed. BS are seeking additional information in respect of one of the bids. Moreover, the Department has been informed that further talks are due to take place shortly on the possibility of a Cuban order which could affect the assessment of the bids.

In these circumstances, BS and their advisers have not yet been able to provide Ministers with final advice. Ministers recognise that a decision needs to be taken as quickly as possible but are concerned to ensure that every avenue has been fully explored.

cc Pk
✓



NBPM

REC

Y.

Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon Nicholas Ridley AMICE MP
Secretary of State for the Environment
Department of the Environment
2 Marsham Street
London
SW1P 3EB

2 November 1988

Dear Secretary of State

PROPOSED ENTERPRISE ZONE AT SUNDERLAND

Thank you for copying to me your letter of 24 October 1988 to Tony Newton.

We are agreed that there is to be an Enterprise Zone at Sunderland if the NESL yards close. I understand your and Tony's wish to use Enterprise Zone designation to assist in the regeneration of the shipyard sites. I would be willing to be flexible in the selection of sites to be designated: some shipyard sites may be included within the agreed 150 acre total. And I am content with your suggestion of a study commissioned by the UDC to report by the end of the year provided that the eventual Enterprise Zone is within the terms of the earlier proposal which I agreed, namely that there is a single designation of no more than 150 acres and the costs are met within existing provision.

I fully share your hope that it will never be necessary again to have to use Enterprise Zones. In order to buttress this policy stance I would hope you can avoid an extension of the designation of the Sunderland Enterprise Zone by instructing the UDC to complete this part of its study quickly. The test of Tony's initial announcement might then refer not only to the need to obtain EC clearance, but also to the need to await the UDC's study before agreeing on detailed boundaries.

I note that you suggest returning to the question of possible resources for clearance of the shipyard sites in the 1989 Survey. I would be willing to consider a proposal to re-adjust your priorities within the Urban Group to give the UDC additional resources if justified in order to undertake the reclamation of

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the shipyard sites. However, since we have only recently considered overall urban provision in the Survey, I believe you should plan on the basis that no additional resources from the Exchequer will be made available to cover these costs.

I am copying this letter to the Prime Minister, Tony Newton and other members of E(UP), Paul Channon and Sir Robin Butler.

Yours sincerely
Cairns Evans

JOHN MAJOR

approved by the Chief Secretary
and signed in his absence



dti

the department for Enterprise

CONFIDENTIAL

The Rt. Hon. Tony Newton OBE, MP
Chancellor of the Duchy of Lancaster and
Minister of Trade and Industry

Rt Hon Malcolm Rifkind QC MP
Secretary of State
Scottish Office
Whitehall
LONDON
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NBAW
RIG
1/11

Department of
Trade and Industry

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Telex 8811074/5 DTHQ G
Fax 01-222 2629

Direct line 215 5147

Our ref

Your ref

Date 31 October 1988

Maledon

BRITISH SHIPBUILDERS AND THE NORTH EAST *flap*

Thank you for your letter of 18 October. Although I fear the absence of suitable alternative powers may still mean my enterprise package for Sunderland will have to be provided through a subsidiary company of British Shipbuilders, I am quite clear that the new company will be limited in application to the area covered by Sunderland Borough Council and that it will not have a role elsewhere.

Nor will it be presented as connected with British Shipbuilders. All shades of opinion in Sunderland have stressed to me how important it is that my package should be divorced as far as possible from British Shipbuilders and be seen as home grown. To that end, I have it in mind to subsume the identity of the measures under the wing of an initiative for Sunderland being spearheaded by local business people. Given all this, and the key importance of the Sunderland yards for the town as perceived locally, I am confident that I shall be able to meet your concerns.

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the department for Enterprise

In the light of this I doubt there is any need to pursue the issue of funding possible remedial measures in Scotland. I should say, however, that my predecessor made abundantly clear on a number of occasions that this would be your responsibility. Having just settled a PES round where my bid for a package of measures related solely to Sunderland, I could not now consider diverting some of this to meet your concerns. If you do not think such measures would be sufficiently important to fund at the expense of your own programmes, that is your decision. But as I say, I hope this issue will not arise.

Copies of this letter go to the Prime Minister and the members of E(UP) and to Sir Robin Butler.

TONY NEWTON

NAT IND

Shipbuilding pt 15

dti

the department for Enterprise

cc ptt
CONFIDENTIAL

The Rt. Hon. Tony Newton OBE, MP
Chancellor of the Duchy of Lancaster and
Minister of Trade and Industry

Rt Hon Nicholas Ridley MP
Secretary of State
Department of the Environment
2 Marsham Street
LONDON
SW1P 3EB

**Department of
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Our ref

Your ref

Date 31 October 1988

NBAM

REC

1/11

John Hicks

NORTH EAST SHIPBUILDERS LTD SUNDERLAND

Thank you for your very helpful letter of 24 October. *Ref*

I would certainly like to make reference to the establishment of the Enterprise Zone in the statement I now plan to make on 3 November. I also appreciate the caveat about your urgently consulting the European Commission. However, provided we are prepared to assure Peter Sutherland that we shall take steps to avoid windfall gains and that the Commission's principles on the cumulation of aids is observed, I am confident we should have no difficulty in securing the Commission's agreement. These were, I believe, conditions the Commission required in order to approve the Inverclyde Enterprise Zone.

Subject to these points, I have Peter Sutherland's assurance that he will do all he can to help, given the reduction in excess merchant shipbuilding capacity which closure of the shipyards would help to achieve.

You raise two related points about the future of the land presently occupied by the yards. Normal practice is for BS to meet the costs of disposal, including any necessary clearance, from disposal proceeds. I am prepared for BS to do this at

OC4ABH



the department for Enterprise

Sunderland. But BS have always disposed of surplus facilities to their commercial advantage and you are suggesting a study on future uses for the sites, including the point about the two stage EZ.

I have no difficulty with a study which leads to well planned development in Sunderland. However, especially as you suggest it should be conducted by the UDC, I am sure it is best regarded and paid for as in the interests of your Department. In return, I am happy to put it to BS that they should be prepared to co-operate, even though this may eventually result in marginally higher closure costs.

I am copying this letter to the Prime Minister, members of E(UP), Paul Channon and Sir Robin Butler.

TONY NEWTON

OC4ABH



NAT IND

Shipbuilding pt 15

cc pd



NB Am
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27/10

Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon Tony Newton OBE MP
Chancellor of the Duchy of Lancaster
and Minister of Trade and Industry
Department of Trade and Industry
1 - 19 Victoria Street
London
SW1

26th October 1988

Dear Tony,

BRITISH SHIPBUILDERS AND THE NORTH EAST

Thank you for your letter of 24 October 1988. I have also seen a copy of Malcolm Rifkind's letter of 18 October 1988 to you.

I agree in principle with your decision that NESL must close, and that there should be an early announcement subject to the further consideration mentioned in your letter of yesterday. I am content with the line you propose to take, subject to your officials clearing the text with mine.

I see considerable attractions in your and Malcolm's suggestion that the enterprise company should, if this is possible, be run as an entity that is separate from BS, and not as a subsidiary of the Corporation provided there are suitable powers available to DTI to establish such an independent company. It is clearly important to ensure that the company is seen to be a response to the particular employment problems of Wearside, following the closure of NESL, and not as a response to all the redundancies caused by closure of BS facilities. Your and Malcolm's proposal seems to be a way of achieving that and I hope it can be implemented.

I am also concerned to ensure that we exercise a proper degree of control over the implementation of these measures. This would, I think, also be easier to achieve if the company were a separate entity, reporting directly to your department, and not a subsidiary of BS.

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Whatever form the company takes, I would not expect to make available additional Exchequer resources beyond those agreed in the Survey to fund enterprise company consequences of British Shipbuilders' redundancies throughout the UK.

As regards new or extended enterprise zones, it is announced Government policy that a general extension of the experiment is undesirable and it is important that we avoid undermining this policy. They have proved costly in the past and as I said earlier I would not expect further zones to be designated.

I am copying this letter to the Prime Minister, Malcolm Rifkind, members of E(UP) and to Sir Robin Butler.

Yours Ever,
John
JOHN MAJOR

1122
18/10/84

NAF FND: *Shipbuilding Policy A 15*

PA

CEW

The Rt. Hon. Tony Newton OBE, MP
Chancellor of the Duchy of Lancaster and
Minister of Trade and Industry

Rt Hon John Major MP
Chief Secretary
HM Treasury
Parliament Street
LONDON
SW1P 3AQ

Prime Minister²
As I reported to you
at lunchtime.

Department of
Trade and Industry

1-19 Victoria Street
London SW1H 0ET

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Direct line 215 5147
Our ref
Your ref
Date 25 October 1988

REC
25/10

MS

Dear Chief Secretary,

BRITISH SHIPBUILDERS: NORTH EAST SHIPBUILDERS LIMITED

(with PG?)
In my letter of yesterday I said that I expected to announce the closure of the NESL yards tomorrow, Wednesday 26 October. I explained that only a last minute development of an unexpectedly significant kind would lead me to change this plan.

Last night British Shipbuilders received an unsolicited amendment to one of the bids which modified the terms in a way which could be presented by the bidder as a substantial improvement. An announcement tomorrow would be criticised as providing evidence that we had already made up our minds and were not even prepared to consider substantial improvements. This line is already being run hard in the local press in the North East and follows on the reported emergence of further possible orders the same bidder now anticipates from a member of his consortium.

Accordingly, I have asked John Lister to ensure that each of the bidders is given an opportunity to offer final amendments so that I can fairly claim that every avenue has been explored. The BS advisers, Lazards, have invited material by noon on Friday 28 October. This is with a view to a statement on Thursday 3 November.



the department for Enterprise

I do not expect for one moment that I shall wish to change my conclusions from those set out in my letter of yesterday. I do however, think it is important to demonstrate that we are thoroughly exploring all the possibilities.

I should also emphasise that there is no prospect of any further delay beyond Thursday 3 November. As I reported yesterday, the Cubans, on whom two of the bidders are relying for a future workload for NESL, have asked for a letter of intent by 10 November. To wait until after 3 November would take us beyond when a preferred bidder would have sufficient time in which to provide the required letter.

I am copying this letter to the Prime Minister, Norman Fowler, Malcolm Rifkind, Tom King, Nicholas Ridley and John Wakeham and to Sir Robin Butler.

Your sincerely,

Peter Smith

PP TONY NEWTON

(Approved by the Chancellor
and signed in his absence)

dti

the department for Enterprise

→ RA

CPH

CONFIDENTIAL

The Rt. Hon. Tony Newton OBE, MP
Chancellor of the Duchy of Lancaster and
Minister of Trade and Industry

Rt Hon John Major MP
Chief Secretary
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Prime Minister²
Confirms the intention
to proceed with a
clear announcement
on Wednesday.

Direct line 215 5147
Our ref
Your ref
Date 24 October 1988

RA16
24/10
Yes me

Dear Chief Secretary,

BRITISH SHIPBUILDERS: NORTH EAST SHIPBUILDERS LIMITED

The closing date for bids for North East Shipbuilders Limited (NESL) was 30 September. You will be aware from my minute of 22 September to the Prime Minister that I had expected that none of the bids would prove satisfactory. This has indeed proved to be the case. It is just possible there may be further developments in the course of tomorrow but unless these are radically different from what has happened so far I see no alternative to announcing the closure of the NESL yards. I propose to do so in a statement in the House of Commons on Wednesday 26 October.

Bids Received

BS received four bids for NESL. Together with their advisers, Lazards, they examined each of the bids carefully and held meetings with each of the four bidders. John Lister has now written to me endorsing Lazards' conclusion that, on financial and commercial grounds, he could not recommend that any of the four bids should be accepted.

TN8AAG

None of the bids comes from a major industrial concern or similar group with significant resources. In an industry as cyclical as shipbuilding and with NESL having virtually no further work in hand, there must be a genuine doubt as to whether any of the bidders could withstand the difficult times that will inevitably come over the next few years. We have previously made clear that any sale must be expected to lead to a secure long term future for the yards. There can be no justification for prolonging the current uncertainty. On this basis alone, all four bids could be turned down.

In addition, there are significant further problems with each of the bids. One of them depends on securing licences from MAPP for deep sea dumping of waste. This would take time to obtain and in any event I understand MAPP have strong reservations. A second bid is from a small local ship repair operation who would want BS to sack all of its remaining 2,000 or so employees and would then recruit as required. Clearly this would give no real future for the vast majority of those who would be affected. The third bidder owns a successful but fairly small industrial group in the Midlands with interests in engineering and paper and carpet manufacture. He has no experience of shipbuilding, would want BS to make about one half of the workforce redundant and, like the other bidders, could give little assurance of further orders. Finally, there is a bid from a Dane who has links with the Danish entrepreneur Johansen who placed the abortive ferry order with NESL. He has experience in shipping and shipbuilding. He has, however, not revealed the full extent of his financial resources or those of his backers. This, together with his links with Johansen, does not inspire confidence. Again he would expect BS to make about one half of its workforce redundant.

My officials have been closely involved in considering the bids. They have also received comments from my Department's advisers, BZW. The conclusion, with which I agree, is to concur with the advice of BS and Lazards.

Cuban Order

The last two bids to which I have referred have also made it a condition that they secure an order from Cuba for ten new cargo vessels. At the end of last week, the Cubans informed us that they were looking for a letter of intent by 10 November. It is widely perceived in Sunderland that the future of the yard depends on the order being secured. The 10 November deadline reinforces the case for an early announcement.

The Cubans also told us they would expect to pay no more than \$16m per vessel (£9.2m). Our previous expectation had been that an acceptable price would be around £10m. Indeed, one of the bidders has assumed taking the order at £10.2m per vessel. It is not clear how far this is a negotiating position on the part of the Cubans but it makes it even clearer that BS would never have been successful in taking the order themselves. It also makes it less likely that a private sector bidder could have taken the order either.

European Aspects

I discussed the position with Commissioner Sutherland last week. He said that in his judgement at least two, and possibly all, of the four bids would be likely to require a formal procedure under the Treaty of Rome whereby Member States would receive details and be given an opportunity to raise objections. Such a procedure typically takes up to 6 months. This would of course last until well after the Cubans are requiring not only a letter of intent but also to have placed the order. Moreover, Sutherland's view is that two of the bids would almost certainly result in a negative decision after having been taken to a procedure.

When I saw Sutherland I pressed him to agree, in the context of the expected decision on NESL, to be as helpful as possible in clearing notification of the terms of the package of measures for Sutherland and the disposal of Appledore, Clark Kincaid and, if possible, Ferguson. He said that he would. There is therefore a reasonable prospect that all of these issues will have been cleared through the EC by about the end of the year.

Package of Measures

We agreed in the PES round details of funding a package of measures for Sunderland along the lines agreed at the Prime Minister's meeting on 31 March. As you know, the package includes counselling, training and placement services for all those who are made redundant at the yards, a set of enterprise activities on a more intensive scale than was associated with previous closures, and a programme of factory building to be funded and carried out by English Estates. In addition, we expect there to be an Enterprise Zone, although as Nick Ridley has explained in his letter to me of earlier today this is subject to approval by the European Commission.

I shall present the package in very positive terms. We have taken the view that shipbuilding does not offer a secure long term future and we must emphasise the way in which the package

will promote the growth of new job opportunities. Here, as elsewhere, I am also keen to build on the role of the private sector. With my encouragement a group of Sunderland businessmen have been planning an initiative aimed at stressing the positive and forward-looking aspects of industrial and commercial opportunities and to come forward with specific announcements in the near future. I am glad to say that they have agreed to make the new enterprise company a joint venture with ourselves. The precise mechanism still remains to be decided but I hope it will be possible to set up an independent company not associated with BS, thus meeting the main concern in Malcolm Rifkind's letter to me of 18 October.

I trust you will be content for me to proceed with an announcement on 26 October.

I am copying this letter to the Prime Minister, Norman Fowler, Malcolm Rifkind, Tom King, Nicholas Ridley and John Wakeham and to Sir Robin Butler.

Yours sincerely,
Peter Smith

PP TONY NEWTON

(Approved by the Chancellor
and signed in his absence)

NAT 120.

Shipbuilding

At 15



CPS



2 MARSHAM STREET
LONDON SW1P 3ES
01-212 3434

My ref:

Your ref:

The Rt Hon Anthony Newton MP
Chancellor of the Duchy of Lancaster
Department of Trade and Industry
1-19 Victoria Street
LONDON
SW1H 0ET

NBM 24 October 1988
ALG
W/10

Dear Tony

NORTH EAST SHIPBUILDERS LTD (NESL) SUNDERLAND

at Harp 14
You copied to me your minute of 22 September to the Prime Minister following your visit to Sunderland. I shall do all I reasonably can within my existing resources to bring relevant programmes to bear on regenerating Sunderland if closure becomes inevitable.

If it does become necessary for you to make a statement outlining a package of measures to assist Sunderland I am sure it would be right to include a reference in that statement to the Enterprise Zone (EZ) which we agreed earlier should be established in the event of closure and which I firmly intend to proceed with. The legal procedures for this are complex and include getting clearance from the European Commission as the first step; their agreement cannot be taken for granted. I suggest therefore that your statement says no more than that I am urgently consulting the European Commission on a proposal to establish an EZ in Sunderland. We shall not be able to say anything more until I have cleared my lines with Brussels when I would aim to make a more detailed announcement setting out my proposals for the Zone.

I would also like to raise with you the future of the land currently occupied by the NESL shipyards. I understand that you take the view that, in the event of total closure, priority should be given to clearing the yards rather than letting them remain as a relic of a past industrial age. I can see the force of that and I want to be helpful if I can. We must not however underestimate the time such a clearance operation might take or the costs that could be involved. The shipyards lie in the UDC area but no provision for their clearance has been made in the UDC's budget or indeed in any of my other programmes, nor is there any prospect that I could find resources for this purpose from within the public expenditure totals I have now agreed with John Major. I assume that you are in a similar position.

There is an important related point concerning the land to be designated as an EZ. Treasury have agreed an EZ of up to 150 acres. We have reviewed our earlier proposals and have now firmly identified about 110 acres of vacant land suitable for inclusion in the EZ. The shipyards cover some 100 acres of land. At this

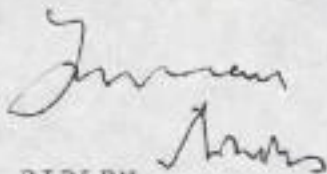


stage, it is unclear how quickly the sites would be vacated. It is also not known how much of the shipyard land could be brought back into economic use at an acceptable cost, when this could take place and at what cost. My officials will discuss with Treasury whether, within the spirit of the earlier approval, sufficient developable land can be identified in the shipyards, to allow an extension of the EZ that could keep within a total of 150 acres. We would need to ensure that the public sector costs were not wholly out of proportion with the original proposals for the Zone and that there were good prospects of levering in substantial investment by the private sector.

Further work clearly needs to be done before any new commitments can be considered. We should make a virtue of that necessity. I would therefore like to suggest that your statement refers not only to the consideration of an EZ but also announces an urgent study of the future potential uses of the shipyard sites. The terms of reference of this study would be agreed between us. Subject to Treasury agreement, amongst other options to be considered we should include a possible extension of the EZ (to come into effect at a later date by a separate order) to cover appropriate areas of the shipyards. The UDC are the obvious body to organise this study which could be completed by the end of the year. Resource provision would properly be a matter for consideration in the 1989 PES round. Certainly I could give no commitment myself at this stage and I think we shall both need to look long and hard at the figures when we get them.

In view of Malcolm Rifkind's letter of 18 October, I should comment briefly on John Major's expectation in his letter of 28 September that the proposed Sunderland zone will be the last to be designated. The policy, which I announced early this year, certainly recognised that enterprise zones would only be designated in future in very exceptional circumstances where other, more cost-effective measures, were considered insufficient. We have agreed that Inverclyde and Sunderland are such cases. But we cannot rule out the possibility that other cases might arise and the option of using enterprise zone incentives must be retained. *Although I hope it will never be necessary again.*

I am copying this letter to the Prime Minister, members of E(UP), Paul Channon and Sir Robin Butler.



NICHOLAS RIDLEY

NAT ind: Shipbuilding
Pt 15





MINISTRY OF DEFENCE
MAIN BUILDING WHITEHALL LONDON SW1A 2HB
Telephone 01 218 6328 (Direct Dialling)
01 218 8000 (Switchboard)

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C/Hover
nbpm

PARLIAMENTARY UNDER SECRETARY OF STATE
FOR DEFENCE PROCUREMENT

USofs(DP) 21/1/13

21 October 1988

1 New 10/13

My officials have agreed with yours the text of replies to an arranged PQ announcing the invitation of tenders for the Aviation Support Ship (ASS) and to questions from Mr Taylor on the position of Harland & Wolff as regards MOD work, both to be answered on Monday.

We have agreed to your Department's request that, for presentational reasons, we should say that consideration will be given to allowing H&W to enter the competition for the ASS at a later stage, once we know the outcome of your consideration of proposals for the privatisation of the yard.

I am, of course, happy to go along with this request but it does need to be clearly understood by all concerned that prime contractors have only nine months in which to complete their proposals to meet our comprehensive requirements in conjunction with their partners and sub-contractors. H&W will need to enter the competition soon if they are to have sufficient time in which to find the right associates and put together a bid in which my department could have faith. There is absolutely no question of our extending the time allowed for the receipt of bids.

This position should be made clear to H&W and to those companies, such as BAe, who have in the past expressed interest in combining with H&W to bid.

I am copying this to Number 10 Downing Street, and to Colleagues in HM Treasury, the Department of Trade and Industry and the Scottish Office, and to Sir Robin Butler.

(TIM SAINSBURY)

Peter Viggers Esq MP
Parliamentary Under Secretary of State
for Northern Ireland
Northern Ireland Office
Whitehall
LONDON
SW1A 2AZ



SCOTTISH OFFICE
WHITEHALL, LONDON SW1A 2AU

CONFIDENTIAL

The Rt Hon Tony Newton OBE MP
Chancellor of the Duchy of Lancaster
Department of Trade and Industry
1-19 Victoria Street
LONDON
SW1

18 October 1988

NBPM at this stage.

Dear Tony,

*REC
18/10*

BRITISH SHIPBUILDERS AND THE NORTH EAST

You sent me a copy of your minute of ^{for PTT4} 27 September to the Prime Minister about your recent visit to North East Shipbuilders Limited.

There is one matter arising from your report on which I would be grateful for your co-operation. The package of remedial measures you have been preparing for use if NESL closes includes an enterprise company. Kenneth Clarke envisaged this as a British Shipbuilders subsidiary, but was not prepared to let it operate in Scotland unless I funded the Scottish operations. It is of course not my responsibility to fund remedial measures which are so specific to a particular industry for which another colleague is responsible. If it becomes necessary to set up an enterprise company, however, it will be difficult for any of us to defend its absence from Scotland if it is established as a BS subsidiary and in due course there are job losses at any BS or former BS operation in Scotland. There are various initiatives in the shipbuilding areas in Scotland which I may use to deal with the wider effects in the local economies concerned. I would have preferred to have had the enterprise company to help directly with counselling and retraining for those who may lose their jobs but not if I have to fund it at the expense of my own programmes. I would therefore suggest that, if you proceed with the enterprise company proposals, you set it up as an independent company specific to the NESL position and not associated with British Shipbuilders. This would contain the political pressures on both you and me to extend its work to Scotland in the future. If you find you cannot do this then I would have to insist that the resources of the company should be available - without any additional contribution from Scottish Office funds - to assist with the consequences of British Shipbuilders redundancies throughout the United Kingdom.

I also want to comment on John Major's letter of 28 September to Nicholas Ridley about the enterprise zone proposal for Sunderland. John says he expects this to be the last zone to be designated. When we reviewed our policy on this matter last year, however, it was agreed to retain enterprise zones as one option for dealing with particularly severe

difficulties, and I certainly intend to keep that option open if a major closure were to arise in the future in Scotland. In addition, I might well consider an extension of the zone in Inverclyde if there are unfavourable developments in relation to the disposal of the BS subsidiaries there.

Copies of this letter go to the Prime Minister, the members of E(UP) and to Sir Robin Butler.

*Yours ever,
Malcolm*

MALCOLM RIFKIND

NAT IND: Shipbuilding

PTIS.





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P 03237

PRIME MINISTER

JAMES MACKIE AND SONS LIMITED, HARLAND AND WOLFF PLC
AND SHORT BROTHERS PLC

E(A)(88)46

DECISIONS

It is clear from Mr King's paper that the future for both Harland and Wolff and Shorts remains bleak. The Government faces substantial expenditure on both companies, whether they close or continue operating to some extent. The main issues to consider are how negotiations with potential purchasers of these companies should be handled, and whether a firmer timetable for decisions should be set than Mr King has so far proposed.

2. You may wish to consider the businesses in the order of Mr King's paper:

i. Mackies. No immediate decisions are needed. Mr King hopes that he has found a buyer. The Government will need to provide a dowry;

ii. Harland and Wolff. The talks with Mr Tikkoo drag on, and two more tentative buyers have appeared. The main questions are whether a deadline should be set on further negotiations with Mr Tikkoo and what attitude should be taken to these other buyers. There is also still the same underlying question of what should be done with Harlands, and how should its remaining work be handled, if no disposal materialises;

iii. Shorts. The main issue is how long Mr King should be allowed to pursue the strategy of a sale of the complete business, favoured by the Shorts board, before offers for the remaining viable parts of the business are taken up. The

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contingent liabilities potentially falling to Government if Short's aircraft and aerostructures businesses close may well be very expensive.

3. In order to keep up the pressure for early progress, you could ask Mr King to report back to E(A) on all three businesses before Christmas. This could be particularly important in the case of Shorts, if there is to remain a chance of selling off parts of the business in this financial year. (The progress report could also cover Mr King's plans for privatising Northern Ireland Electricity, which was agreed by E(A) in July.)

4. E(A) needs to settle External Financing Limits (EFLs) for Harland and Shorts for 1988-89. We understand that the Treasury are likely to agree to Mr King's proposals of £62.3 million for Harlands and £70 million for Shorts.

BACKGROUND

5. E(A) last discussed these three businesses on 13 July. On Mackies, it was agreed that Mr King could offer a dowry to a private sector buyer in order to secure a sale, and that he could take limited temporary steps, from resources within the Northern Ireland block, to ensure the company's survival whilst negotiations on its sale proceeded. On Harlands, E(A) were highly sceptical that negotiations with Mr Tikkoo would be successful, but agreed that these negotiations should be pursued for the present. On Shorts, it was agreed that the objective should be privatisation at the earliest possible opportunity, with any new private sector management becoming responsible for sorting out the company's business. Mr King was asked to report back to E(A) in September with his plans for privatisation, and in the meantime to discuss with the Chief Secretary the minimum amount of Government support likely to be needed to make privatisation practicable.

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ISSUES

Mackies

6. There appears to be a reasonable prospect that Mackies can be sold to a private sector buyer, at a cost in terms of Government support within the figure of £20 million previously contemplated. We have been told that disposal may be possible in the next two months; but this may prove optimistic, given past experience. At present Mr King is seeking to resolve difficulties created by the trustees who presently hold the shares of Mackies on behalf of its employees. Such shares would of course be worthless without future Government support. The package of support envisaged for Mackies is understood to be along traditional regional assistance lines. Mr King is not asking for any decisions to be taken about Mackies at this meeting. You may wish simply to:

i. obtain confirmation from Mr King that the provision of a dowry would not be expected to cause problems with the European Commission. You asked him to clarify this point at E(A)'s meeting in July;

ii. repeat that, as previously agreed, he will need to clear the detailed support package with the Treasury when he is ready to finalise it.

Harland & Wolff

7. Following Ministerial correspondence, a counter offer was put to Mr Tikkoo a couple of weeks ago in connection with his bid to acquire Harlands and build a large cruise ship there (the P3000). The terms of the counter offer were within the precedent set by the disposal of Govan shipyard to Kvaerner. Even this counter offer would require the Government to write off Harland's existing debts of £266 million and to provide around £200 million in support for the P3000 project. However, the counter offer was considerably short of what Mr Tikkoo had first requested, and it is not clear if he will wish to take negotiations any further. There is a rumour that he has been offered

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better terms in France, which do not require him to purchase the relevant yard. Mr King may say that he would face major political difficulties in Northern Ireland if Harlands were seen to close because the French Government offered Mr Tikkoo larger subsidies. Since July two more tentative bidders - Bulk Transport and UM Holdings - for Harlands have appeared. Both, however, wish to build relatively standard vessels which can be constructed much more cheaply in the Far East. Mindful of this, the Harlands management have a strong preference for building Mr Tikkoo's ship. You will wish to ask Mr King for his latest assessment of the prospects for a successful disposal of Harlands.

8. The following issues may arise in discussion:

a. deadlines. The Chancellor is expected to press for a deadline to be set for conclusion of negotiations with Mr Tikkoo, of perhaps a month's time. Subject to what Mr King says, you may well wish to consider this;

b. other bidders. You may also wish to reach a decision in principle on whether it is wise to pursue bids requiring vessels to be constructed in direct competition with Far Eastern yards. It is hard to see why private companies should be interested in acquiring Harlands for this purpose unless they hoped to receive large Government subsidies;

c. the future if the yard is not sold. Harlands will need to remain open for at least two years if the AOR is to be completed. Major decisions are likely to have to be faced next year when steel fabrication on the AOR has largely been completed. In the meantime you may wish to see a further gradual rundown of the yard as work reduces. Over 500 redundancies were implemented during the summer. You may wish to ask Mr King what plans he has for managing the rundown of Harlands if no satisfactory buyer emerges. Mr Younger may wish to comment on the implications for completing the AOR in these circumstances.

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9. On Harland's current financial position, the note by officials attached to Mr King's paper gives a breakdown of Mr King's proposed EFL for Harlands in 1988-89 of £62.3 million (an amount of £1.7 million for work in progress on the AOR has been added to the figure of £60.6 million in the note). This works out at around £20,000 per employee this year. We understand that the Treasury hoped for a somewhat lower figure than £62.3 million, but that they regard this as realistic and are therefore likely to be prepared to accept it. Mr King will ask E(A) to endorse this figure.

Shorts

10. Following the controversy with the Shorts board when privatisation of the company was announced in July, Mr King agreed that an attempt would be made first to find bidders for Shorts as a whole. You will wish to hear Mr King's latest assessment of the prospects for a successful sale. The main issue is how long this opportunity should be allowed to last, given the Chief Secretary's objective of completing a disposal in this financial year. We understand that Mr King's present plan is for definite expressions of interest to be invited once the accountants report on Shorts has been made available in a month's time, and then for a shortlist of bidders to be drawn up by Christmas. The Chancellor may wish to tighten up this timetable, and to obtain a clear commitment from Mr King to it.

11. The Shorts board wish to develop a new aircraft, the FJX, in order to keep the aircraft section of their business in being. In July E(A) were highly sceptical about whether there was any future for the aircraft business. Mr King may say that one complication of a complete sale as the board wish is that time will be required to find partners in the development of the FJX. However, such partners are only likely to come forward when it is clearer who Shorts' new owner might be. You may wish to press Mr King on whether there can be any justification for Shorts embarking on the development of a new plane, even in partnership. Any such project is likely to require a substantial amount of Government launch aid. Lord Young or Mr Newton may wish to comment about the potential implications for launch aid applications from other British aircraft manufacturers. Mr King may

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argue that the test for whether launch aid should be provided in Northern Ireland should be whether Short's new owners would be prepared to risk substantial sums of their own money in a new development, alongside the Government. If you concluded that the option of developing the FJX is unrealistic, even in the special circumstances of Northern Ireland, then you may conclude that the time devoted to pursuing this option should be minimised, even though this would inevitably cause major difficulties with the Shorts board.

12. The case for asking Mr King for a further progress report to E(A) before Christmas is to allow decisions to be taken that the company has to be rationalised, or sold in parts, if no satisfactory bidders have emerged by then for the whole business. This report should discuss the implications of requiring European Commission clearance for any disposal. Preliminary indications suggest the Commission will be much more tolerant of a European purchaser than an American one (particularly if it is Boeing). You may wish to ask whether the Commission is likely to be a difficulty.

13. Mr King's paper provides little information about the total potential costs of disposing of Shorts. In addition to repaying Shorts past debt of some £300 million, a dowry to fund any necessary redundancies and possibly launch aid will also be required. The contingent liabilities of the aircraft and aerostructures business are also substantial, and it may not be possible for all these to be passed on to a private buyer. You may wish to ask Mr King to cover the overall financial consequences of a disposal in his next E(A) report.

14. Shorts have proposed an EFL for 1988-89 of £70 million. Borrowing is cyclical to some extent, but it has currently reached £110 million since April and is expected to peak at £131 million in mid-November. There must be some doubt whether borrowings for the year will get below £100 million again. Nevertheless, Mr King believes that it is tactically correct to set Shorts EFL at the £70 million level forecast by the company, to keep the pressure on them to reduce borrowings. We understand that the Chancellor is advised to endorse this judgement and, on that basis, you may be prepared to

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conclude that Shorts EFL for 1988-89 should be set at £70 million. Before doing so, you may wish to ask Mr King whether he is now more satisfied with the company's financial controls than he was in July, and whether he still contemplates starting negligence actions against Price Waterhouse, the company's auditors, or Touche Ross, his own financial advisers.

HANDLING

15. You may wish to ask the Secretary of State for Northern Ireland to introduce his paper. The Chancellor of the Exchequer will wish to respond. The Secretary of State for Defence has been invited for the discussion of Harlands. He may wish to comment on the issue raised in the July meeting about whether Harlands could be sold to a foreign owned company when it was in possession of defence information in connection with the construction of the ADR. The Secretary of State for Trade and Industry or the Chancellor of the Duchy of Lancaster may wish to comment on the possible application of Shorts for launch aid. Other Ministers may wish to contribute to the discussion.

R.T.J.

R T J WILSON
Cabinet Office
5 October 1988

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PRIME MINISTER5 OCTOBER 1988MACKIES/HARLANDS/SHORTSMackies

It is good to hear that there is one potential buyer showing some enthusiasm. Any viable deal will probably require Government funding which can only be justified on political grounds. Furthermore it is essential that it is a genuinely private solution which emerges. One earlier proposal placed a commercial bank in the false position of appearing to finance Mackies while its risks were totally underwritten by government. This is merely disguised nationalisation and Tom King should be disabused that any final solution of that kind will be acceptable.

The original Government investment mentioned was £20 million in order to render the business 'commercially viable'. Your own proposal was to tranche any Government investment so that the benefits of the initial amount would have to become evident before anything further was ventured. It might be appropriate to remind Tom King of that in any encouraging remarks that are made. Nevertheless Mackies appears to be the brightest spot in a very gloomy picture.

Harlands

It is no surprise that the Tikkoo deal is proving hollow. It was most improbable that Tikkoo could make economic good out of Harlands without enormous Government subsidies. His background gives no indication that he could become a chief executive capable of giving Harlands hope of real economic viability. Further dealings with Tikkoo seem both a waste of time and a diversion of effort. It is unlikely that he

can raise private financial backing of the scale required. The Northern Ireland Office should now press on with those other possibilities which the paper mentions under a strict time limit of about two months to produce something viable.

Tom King should be warned against a hastily cobbled deal which technically privatises Harlands without solving any of the yard's underlying problems. This will only rebound on the Government, probably at an awkward time. Far better to face up to closure of Harlands in a planned manner if a genuine sale cannot be achieved in the immediate future. As an interim measure I understand the Treasury will not object to the proposed EFL of £62.3 million.

Shorts

The NIO paper glosses over a major row which Tom King and Paul Viggers have been having with the Shorts Chairman, Rodney Lund. Lund is totally opposed to piecemeal privatisation despite the fact that the only part of the business which has attracted any interest is the missile division. When the Government's intention to sell Shorts was announced in July, Lund accused Viggers of giving a 'totally misleading government briefing' in which management was openly criticised. There was a subsequent vitriolic exchange when Lund even threatened to sue for defamatory statements. - see Annexure A from Lund to King dated 20 July.

Lund further argues that any proposal to sell the missiles division separately (valuations indicate an order of £70 million) will lead to an immediate sit-in by unions at the Aircraft and Aerostructure plant leading to massive liabilities for non-delivery to Boeing. Lund claims that Government has an obligation to meet Shorts' debts because of an assurance given in Parliament by a previous Northern Ireland Secretary of State (cf - the Varley-Marshall

assurances for Rover.) He suggests that the downside risk to Government in pursuing a separate sale of the missile division could therefore be over a billion pounds! The Treasury are highly sceptical about this.

There is no commercial logic in binding the successful missile business, which is physically separate from Shorts main factory with no commonality of manufacture or cross costing benefits, to the heavily loss making aircraft and aerostructure business. The missile division has a turnover of £80 million and 1,500 employees. Its performance is variable but it is basically profitable and has been valued at £70 million. With the Starstreak missile under development, it has a secure medium term future.

By contrast the aircraft (turnover £90 million) and aerostructure (turnover £70 million) activities operate from a single site employing 6,200 people and sharing common resources and facilities. This business is unprofitable and poorly equipped. Shorts management argue that it can only become viable after developing a new short range aircraft - the FJX. This would be a twin jet capable of transporting 44 passengers up to 1,760 kilometres.

Gross investment for this project has been estimated at £500 million of which Shorts would carry £180 million after allowing for investment by partners and sub-contractors. Shorts would want half to be financed by Government launch aid as well as immediate debt restructuring of £300 million for the company overall. This constitutes the nearly £400 million Government investment mentioned in the last E(A) paper which King did not support. Such an amount is of the same order as closure costs and would be in total contravention of Brussels' position on State aid. It is the old Rover argument. Give us the capital for new models and we will set the business right.

You may not wish to bring all this out at E(A) but it is important to be aware of the atmosphere in which King has delegated the privatisation of Shorts to its Chairman and Board as set out in Paragraph 11 of the NIO paper.

Conclusion and Recommendation on Shorts

There has been a very bad relationship between the Shorts Chairman and Northern Ireland Ministers. Instead of firing Lund, Tom King has handed him the business to sell. This is a very high risk strategy, particularly as Shorts is the largest employer in Northern Ireland.

In strict commercial terms the obvious solution is to sell the missile business to a company like Ferranti who have shown interest. Sale of the aerostructures business should also be attempted, perhaps to a consortium of its customers. However, the aircraft business is not viable without a massive Government dowry and the commercial solution must be closure.

It may be that we have no alternative but to stay with Lund for the immediate future, because there may be no one better to take the job. However you should test this assumption very carefully, either with Tom King privately or, if appropriate, during E(A). In my experience, whenever the shareholder abandons its business to a potentially hostile management, no good results. It would be far better if responsibility for privatising the company could be separated from its present management.



GEORGE GUISE

SECRET

ANNEX A

SHORTS

Rodney Lund

E

RL/CMH

July 20, 1988

The Rt. Hon. Tom King MP
Secretary of State for
Northern Ireland
Northern Ireland Office
Old Admiralty Building
Whitehall
LONDON SW1A 2AZ

Dear Secretary of State,

I hardly have to tell you how utterly dismayed I am about the recent leakages to the Press of information confidential to this Company and to read the quite extraordinary and defamatory statements about the Management. A reasonable man might wonder if there was some wish to sabotage the Company.

I think you will agree that the damage to the Company is so serious that I have no option but to write to the Prime Minister for help which I have done today.

Most damaging of all to the Company are the press statements that we have lost £85m in the first quarter. Suddenly the most horrendous thought crosses my mind. Can it be that you have been wrongly briefed? The pre-interest loss for Shorts for the first quarter is in fact some £10m - and this is traditionally our worst quarter. The £85m is simply a measure of our peak cashflow operational requirement and is not unusual for this time of the year.

When we last met I could not understand your remarks about massive haemorrhaging because I knew our quarterly results would not be too far off target. Is it possible that you really thought we had lost £85m? Certainly whoever leaked this confidential figure to the Press must have thought so. It would scare me too much if I thought that recent decisions about the Company might have been predicated by someone in the system who did not know the difference between profit and cashflow.

I enclose a copy of a letter from our lawyers to Mr. Viggers which is self explanatory.

*Yours sincerely
Rodney Lund*

SECRET



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Manop + negs pt 3.

RIME MINISTER

MEETING OF E(A): 6 OCTOBER

Papers for the three Agenda items are in the separate folders.

Item I - Northern Ireland issues

You saw the main E(A) paper - Flag A - over the weekend.

Further papers now enclosed are:

Flag B - Further background to the proposed EFL figures for Harland and Wolff and Shorts. I do not think you need bother with this.

Flag C - Cabinet Office brief - you will want to use this to steer the discussion.

Flag D - A note by George Guise. You will want in particular to read George's comments about Shorts.

There are no major difficulties over Mackies.

On Harlands, you will want to consider

- the latest proposals for a successful disposal
- the deadlines to be set
- the implications of run-down for completion of the AOR
- the proposed EFL.

Shorts is very troubling. George's note describes the very difficult relations between Tom King and the company's management. You will want to consider

- the prospects and timescale for identifying potential bidders, either for the whole business or parts of it;
- whether Shorts should even contemplate developing a new 'plane;
- the European Commission aspects;

- the likely financial disposal; and
- the EFL for 1988/89.

Item II - Amendments to Fair Trading Act

You insisted in earlier correspondence that this should come to E(A).

Over the weekend you saw the initial DTI paper - Flag E. I told DTI that you regarded this as inadequate and they have now provided further material in the letter at Flag F.

Other papers included are:

Flag G - you may like to have to hand the Lord Privy Seal's arguments about the earlier proposal to set aside the hybrid instrument procedure, which Lord Young has now dropped.

Flag H - Cabinet Office brief.

Flag I - Note by George Guise

Lord Young has two proposals still on the table:

- (i) The creation of a new offence of deliberately or recklessly supplying false information to the competition authorities. The Cabinet Office brief (paragraph 9) points out that this follows a precedent already set on gas licensing. You may therefore feel this point can be quickly agreed;
- (ii) the introduction of a general power enabling the Secretary of State to implement recommendations specified in MMC reports.

This is the issue which most concerns you. The Cabinet Office brief fairly sets out both sides of the argument, and highlights the sort of points which have been troubling you. George

Guise, however, comes down strongly in favour of Lord Young's proposal. I think the key points are:

- there is already a general power in relation to prospective mergers. Are you happy to introduce a further general power relating to mergers which have already taken place and to monopolies, on the basis that the power could only be used to remedy or prevent adverse effects specified in the MMC reports?

- can the effects Lord Young is seeking be achieved, without excessive costs, by further elaboration of specific powers?

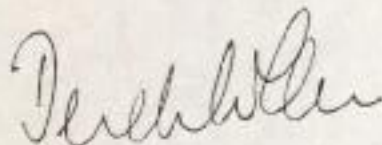
Item III - Nitrates

You have already seen last weekend:

- Flag J - Cabinet Office paper -
- Flag K - Cabinet Office brief -
- Flag L - Policy note.

The only additional paper now available is that by the Minister of Agriculture at Flag M. It encloses a research paper which suggests that the application of nitrogen fertilisers by farmers may not be the main reason for the nitrates problem.

The Cabinet Office brief sets out the main points you will want to work through.



PAUL GRAY

5 October 1988

Duty Clerk.

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copy



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The Rt Hon Tony Newton OBE MP
Chancellor of the Duchy of Lancaster
and Minister of Trade and Industry
Department of Trade and Industry
1-19 Victoria Street
LONDON
SW1E 0ET

NBA
RLB
STO

4 October 1988

Dear Tony.

BRITISH SHIPBUILDERS AND THE NORTH EAST

In your minute of 22 September ^{at Dept} to the Prime Minister you reported on the prospects for NESL in Sunderland and requested contributions for a package of measures in case of a large redundancy there.

My Department is, as you know, already heavily involved in the contingency planning. The Employment Service is standing by to provide employment counselling and Jobclubs, and its Local Enterprise Agency Projects Fund will also be available for specific projects; the Training Agency will offer training and re-training courses; and the Small Firms Service will support the new enterprise company and provide counselling and help for those interested in starting their own businesses, via the Enterprise Allowance Scheme if appropriate.

If therefore the worst comes to the worst and this redundancy takes place, the services of the Employment Department Group will be readily available to the redundant workers.

I am copying this letter to the Prime Minister, the members of E(UP), Paul Channon, and Sir Robin Butler.

Norman Fowler
NORMAN FOWLER

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NAT (NO. Shipbuilding p. 14

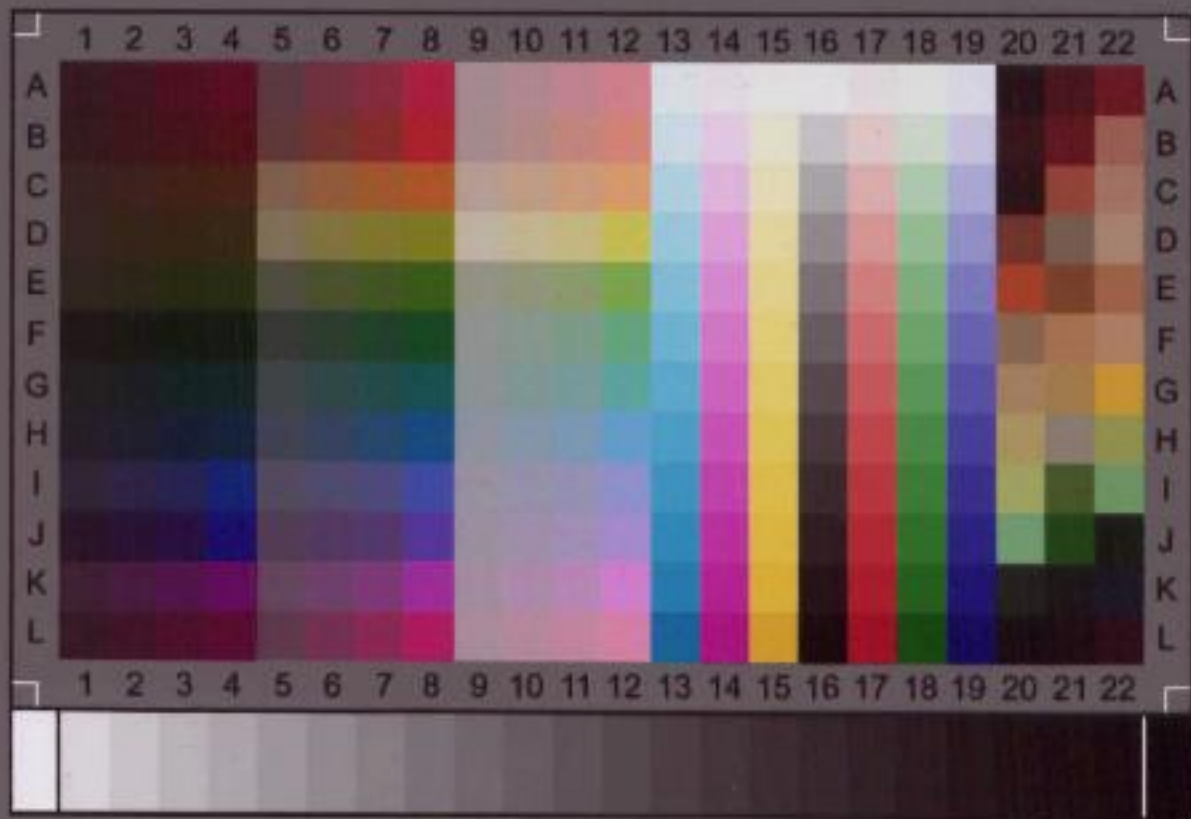


● PART 14 ends:-

PG to PM 30.9.88

PART 15 begins:-

SS/EMP to CCL 4.10.88



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