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PS/ *Secretary of State for Industry*

25 January 1980

Tim Lankester Esq
Private Secretary to the Prime Minister
10 Downing Street
LONDON SW1

Must discuss with Keith

Dear Tim,

A critical situation is looming in connection with BSC finances in 1979/80 and 1980/81. The Department monitors BSC finances and the most recent estimates we received from BSC were prepared early in December. These forecast losses of a little over £300 million for 1979/80 but with BSC still keeping within the external financing requirement of £700 million. For 1980/81, BSC forecast a profit of £45 million after depreciation, interest and a contingency allowance of £110 million but with downside risks of £210 million. A cash requirement of £500 million was to be met by external financing of £450 million plus £50 million from disposals, stocks etc. These figures were presented to the BSC Board in December.

Since December, the part-time businessmen Members of the BSC Board have become increasingly concerned about the credibility of these estimates, particularly those for 1980/81. They asked for the views of BSC's auditors. We shared these doubts and my Secretary of State told the Chairman on 20 December that he proposed to introduce, as from March 1980, much more stringent monthly monitoring of BSC's use of cash. Sir Charles has not yet replied to this letter.

Following these developments, BSC executives have reviewed the estimates with their auditors. The results were presented to the newly constituted BSC Finance Committee, of which Mr Gross is a member, yesterday evening. The revised estimates forecast a loss of £402 million and a cash requirement of ~~£884~~^{£864} million in 1979/80 assuming a 4-week strike or a loss of £427 million and a cash requirement of £888 million if the strike lasts 8 weeks. The external financing requirement this year is £700 million and the difference can be covered either by seeking more money from Government or by deferring March payments into the 1980/81 financial year (which would, of course, worsen the position then).

For 1980/81, the revised estimates (after allowing for the proposed closures at the planned dates) show a loss of £285 million, and a cash requirement of £715 million, ie an excess of £265 million over the external financing limit of £450 million, plus any spill over from 1979/80. The strike and its aftermath explain perhaps a

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third of the difference between the December and the January estimates. Most of the balance is accounted for by the auditors' conclusion that the December "downside risks" should really be part of the central estimate.

In essence, the Finance Committee, including the Chairman, concluded yesterday that BSC were faced with a cash deficit of between £300 and £500 million between now and 31 March 1981 over and above the present external financing limits. (Sir John Buckley considers the deficit could easily be a good deal more.) BSC therefore seem likely to make losses in 1980/81 of about the same order as in recent years despite all the closures and other productivity improvements of which we have been told.

The Chairman told the Committee that this cash deficit could be met in four ways:

- (a) reductions in stocks
- (b) reductions in capital investment;
- (c) disposals of assets, including mainline assets;
- (d) the creation of a "closure account";
- (e) reductions in the interest burden.

Mr Gross said that the Government would not oppose (a), (b) or (c) and there might be opportunity for a minor reduction in (e) through earlier redemption of overseas loans against more Government money - which would involve no net increase in the external financing limit. However, on present instructions, (d) was not a starter if it involved an increase in the limit.

Other Members noted that, while disposal of assets in 1980/81 was a credible cash source for say £50-150 million, disposals did not constitute a reasonable expectation of raising cash of the order of £300-£500 million, since disposal of mainline assets of the kind suggested by the Chairman (Tubes Division, Stainless Steel, Tinsplate and Cumbria) could prove difficult, particularly if prospective purchasers were repelled by the employment terms and conditions of the BSC workforce. Accordingly, the question would arise whether, if the Board accepted the revised estimates, the Corporation could properly go on accepting new liabilities on a "going concern" basis, without an assurance of additional financial support from Government.

In practice the Government has no option but to back the debts of the Corporation. But my Secretary of State envisaged last summer that, if BSC failed to meet the 1980/81 financial target of breakeven which he then set them (itself a less onerous target

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than the Board had set itself, with the previous Government's support, in April 1978), drastic remedial action would be needed. My Secretary of State has not yet had time to consider the detailed implications of this drastic alteration in BSC's circumstances. He thought the Prime Minister should know at once. He intends to give urgent consideration to radical changes at the top of BSC.

Timing will be important. The Department is aware of the new estimates only through Mr Gross's membership of the Finance Committee and has not yet officially received them. The estimates have still to be approved by the BSC Board, which is meeting on Thursday 31 January. The two Government Directors consider that some of the detailed figures are open to challenge and may be a shade pessimistic in some areas but do not dispute their general validity. My Secretary of State clearly cannot act before Sir Charles Villiers has reported to him the outcome of the Board meeting on 31 January. Equally, drastic changes will be difficult while the strike is still on. On the other hand, the Government may well need to act, or at least be ready to do so, before 13 February, when Sir Charles Villiers is due to appear before the Select Committee on Industry and Trade. He will not be able to parry questions on financial estimates if the revised figures are approved by the Board.

In view of the sensitivity of this information, I am copying this letter only to Martin Hall (Treasury), Ian Fair (Employment) and to David Wright.

Yours ever

Ian

IAN ELLISON
Private Secretary