

cc Mr Duguid
✓ D Wright

PRIME MINISTER ²
Not Ind.

To see. We await Sir
Keith Joseph's comments
WELSH OFFICE MS



Thanks
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From The Secretary of State for Wales

The Rt. Hon. Nicholas Edwards, MP.

14 April, 1980.

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Den Prime Minister

I am very much aware that, as a Minister with no responsibility for BSC, it may be presumptuous or out of order for me to express a view about the future of the steel industry. However, I - more than most - have to live with the consequences of BSC's decisions and I have had the opportunity for wide ranging discussions with many people in the industry about its future. I hope therefore that you and Keith will not object to my letting you have my views, which I have set out in the enclosed paper. I have sent a copy to Keith but have not otherwise copied it to colleagues. It may be that the issues I raise are already being considered and that they will in due course be discussed collectively; but if not, you may wish to consider whether some discussion about the points I make would be worthwhile.

I have some reason to think that quite a lot of people in the industry are hoping that we may move along the lines I suggest, and certainly they believe that we cannot go on with the arrangements for the industry unchanged. I hope at least that some of my ideas may be helpful.

hA all will be agreed for at least long time
provide useful debate.

John Evans

Nice

The Prime Minister,
10 Downing Street.

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THE FUTURE OF THE BRITISH STEEL CORPORATION

The ending of the strike at BSC should be the moment for a fundamental reappraisal of the future of the industry and for a fresh start. The financial state of the industry, the condition of its market, the attitude of those who work in it, and political necessity all dictate that. It may be argued that the future of the industry is for management and that the Government should stand aside and let the Corporation sort out its own problems. There are many reasons why this would be an unacceptable line.

The condition of the Corporation's finances will, in any case, involve the Government inevitably in a capital reconstruction of a concern which, without the financial guarantees provided by Government, would now be bankrupt. Were it a private company it would by now be in the hands of the Receiver, and I understand that the cash deficit next year could amount to between £500m and £1,000m. The break even target is surely now not attainable, and even if the Corporation seeks to achieve it and to fund its cash deficit by the sale of assets there must be doubt whether that could be done in the necessary timescale.

At the same time the Government is confronted with the urgent necessity of appointing a new Chairman and Board with the authority to re-establish financial control and to restore the confidence of the workforce which has been seriously damaged.



There may be a temptation to think that a capital reconstruction and the appointment of a fresh Board is all that is required of Government which should then be content to leave it to the new managers to carry out any reorganisation that may be required. I find it hard to believe that new management of sufficient ability would be prepared to undertake the task without assurances about future changes in structure. There is a need to establish terms of reference for the new Board, and to consider the need for legislative changes. Collective agreement by Ministers on these issues is, therefore, a desirable starting point, even if implementation and detail is left to management. In any case there are other reasons for my belief that the Government itself must initiate the fundamental changes that are needed.

The first is both philosophical and practical: it arises from our belief in competition and in the value of small units, both from the point of view of easier management and as a means to more effective financial control. We cannot expect a massive, centrally organised, excessively bureaucratic monopoly, even under new management, to dissolve itself into entrepreneurial, locally managed units involved in genuine competition. Government has created this Frankenstein monster and allowed it to grow: only Government can destroy it.

The second reason arises from the need to regain the confidence of customers and recapture markets. Customer confidence will have been



gravely damaged by the strike; and, if we are to avoid a huge increase in second sourcing and a massive increase in the import bill, it will be necessary to establish quickly and unmistakably that we are creating an industry in which there is genuine competition and alternative sources of supply.

My third reason in the long run may be the most important of all. It is psychological and political. It is the need to give those who work in the industry hope. It would be hard to overstate the sense of desolation and despondency that is present at all levels within the industry at present. As one of the BSC's best managers put it to me: "It would be a tragedy if what has happened was all for nothing. We cannot go back to the same structure, to the same old BSC. We have to take this opportunity to put things right. Let us get the spirit back."

It is not only important for the future of the steel industry itself, but immensely important for our industrial recovery and for our political future to get the spirit back, to restore hope where hopelessness exists, and to emerge from a damaging industrial dispute with a new sense of direction and purpose.

The best companies in the private sector, Sheerness in Kent and Alpha Steel in South Wales, as well as the best parts of BSC - Velindre in the Tinsplate Division, the finishing end at Shotton, some

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sections in Sheffield and perhaps even the heavy end at Scunthorpe, have shown themselves to be first class and able to compete against the best in the world. It is the sense of achievement and purpose found in those places that must be created elsewhere, rather than the bitterness and fear to be found at present in places like South Wales.

The key to recovery is to restore the link between the manufacturing units and marketing, and to reintroduce genuine competition between different parts of the state owned industry, as well as with the private sector. It is almost incredible that a Managing Director of a manufacturing division has no direct responsibility for sales at all. A workforce cannot be expected to co-operate if it can see no direct relationship between its own output, its quality and timing and the sale of its product. There is a growing conviction at every level in BSC that the future lies in the re-establishment of genuine, competing profit centres with control over their own selling and their own labour relations. Whatever the wage negotiating machinery, there needs to be some flexibility at the local level so that there can be a link between output and employees' income as at Sheerness.

There is an aspect of all this that goes well beyond the internal organisation of the BSC. At a time when parts of the United Kingdom, and Wales in particular, are having to face industrial change on a scale that has serious social implications; there is a compelling need to create hope; and I believe that the best way of doing that is to throw down a challenge and to offer the prospect of victory.

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The manner in which BSC came forward with their proposals for demanning, together with their scale and suddenness, and what has been seen as the indifference of Government has created a sense of crisis and a genuine fear of a return to the 30's. BSC's programme (and the NCB's which follows from it) will be resisted at every stage and will be hard to achieve. I believe we could create a wholly different atmosphere and a wholly different prospect if we were to break the BSC up into competing units, and were to create separate units or companies each reflecting a clear identity whether it is that of a region or of a closely associated group of products so that national or regional or professional pride (or all three) can be harnessed to industrial success.

My record in Devolution is sufficiently well known for my political commitment to the United Kingdom not to be called into question; but I believe that almost overnight we could transform the atmosphere and the prospects for the Welsh and for the United Kingdom economies by harnessing the sense of pride and purpose that exists there. That is the prospect we could open up to the employees of BSC as they return to work, and that is a prospect that only the Government could open up. It is a job we cannot leave to BSC; it is, I suggest, a chance we should not miss.



The present Chairman of BSC is moving towards the establishment of separate profit centres, and at the periphery at any rate the new structure is taking shape with the setting up of BSC Holdings, under which the tin-plate, stainless steel and rail making divisions have been grouped; and the possibility of securing private sector participation by way of partnership or other methods is being explored. It remains to be seen whether this represents the start of a genuine move to self standing units, or (as it appears to those employed in the tin plate division in Wales at present) no more than another form of centralisation. The fundamental problems of the steelmaking end, the ponderous central bureaucracy, the relationship between the marketing and manufacturing functions, the management structure and the Corporation's industrial relations have hardly begun to be tackled.

The ideal might be to divide the present corporation into a number of wholly separate state owned companies, each standing on its own feet and each capable of obtaining sooner or later an increasing amount of private sector participation. Certainly I believe we should regard increasing privatisation as a desirable objective in itself and seek to organise the industry in a way that makes that a practical possibility. We should, therefore, consider whether it would be feasible to sub-divide the existing organisation in this way, so that we can do without a central state enterprise altogether. We may conclude that that is not a practical possibility, at least until a later stage, because of the need to allocate capital resources from the taxpayer which Governments are perhaps not equipped to do. (We can hardly saddle such a mammoth task on the NEB as we now envisage it).

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If that were to be the conclusion, we would have to have a holding company; but it need not and indeed must not bear the slightest resemblance to the animal now occupying Grosvenor Place. It should be purely a financial holding company responsible for the capital allocation, budgetary control, financial discipline and appointments of the group. National Steel in the United States is, I believe, about three quarters the size of BSC. It has a holding company about sixty strong and controls five or six operating companies. That is the kind of structure I have in mind.

It might be appropriate that the only full time directors of this body should be the Chairman, Managing Director and Finance Director with the other Directors as part-timers; even a part-time Chairman might be possible with this structure. In this way it would probably be possible to attract people with a proven track record and still active in large industry with a real knowledge of what can and cannot be done in the modern industrial scene.

Whether there is a holding company or not, there is room for considerable variety in the make-up of the operating companies and I am not qualified to do more than suggest some tentative possibilities. Initially there might be six or seven such companies. They should have their own Chairmen and Boards with wide powers and full responsibility for their operations, and even under the holding company structure one would wish to see those Boards include outside Directors and to have extensive authority.



1. The Steel Company of Scotland

This would be based on Ravenscraig which is the best equipped major plant in the country. It has adequate coking capacity, three good blast furnaces of economic size giving it the best iron making installation. It has the best steel plant and casting machines to cover its product range. The Hunterston ore terminal gives it its necessary bulk ore cargoes. However all this plant represents a major financial burden and it remains to be seen whether even in a competitive situation and with control over its own marketing, Ravenscraig could use its equipment to anything approaching capacity and make a profit.

2. The Steel Company of Wales

The problems to be overcome here are considerable, but not insuperable. It is sometimes argued that Llanwern and Port Talbot would not be able to stand up to the competition from Ravenscraig in a market where capacity is likely to exceed demand but Ravenscraig has yet to prove itself and until it does we should not assume that its costs will necessarily be lower. Much of the plant is comparable and of similar age and the blast furnaces and converters are actually smaller than at the Welsh plant. Llanwern probably has the better strip mill and Port Talbot will soon have its concast plant (though if this is under-utilised interest charges and depreciation could add to costs rather than reducing them). There will come a time when the rolling mill at Port Talbot will have to be brought up to date and until the recent crisis BSC was planning to spend a great deal on coke oven replacement at Llanwern but the Port Talbot modernisation could well be put off until an increase in demand justifies it, and there are alternative sources of coking coal available for Llanwern.

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The combination of Port Talbot's steel making capacity and ore handling facilities and Llanwern's rolling mill is quite formidable and there is a good deal of industrial logic in the proposed "dogleg" solution based on this combination. However that has been abandoned in favour of a slimmed down workforce at both plants and, if that solution may be faulted on grounds of industrial logic, it could be worthwhile if it captures the co-operation of the workforce. There can be little doubt that far too little has been done in the past to tackle the problem of overmanning. The quality has generally deteriorated (particularly at Port Talbot) and delivery performance has been unreliable.

It is the faltering performance of the workforce under the present unsatisfactory management structure which is more serious than the problems related to plant and capital investment, yet even that compares well with anything that has been achieved at Ravesraig. Given new management with real responsibility at local level, and a genuinely competitive situation there is a very good chance that South Wales plants will improve performance and regain a substantial share of the market.

The tinsplate operation should be included in the Welsh Company. The Welsh industry was built up on tinsplate and there is a natural link with the Welsh steel making plants, indeed it was their main "raison d'etre". Until the South Wales plants can become competitive it is more sensible that tinsplate should stay in the Welsh Company and provide a steady load on the major plants coupled with more aggressive, locally based marketing to capture a greater share of the tinsplate market.

Shotton is referred to separately.



3. North East Steel Company

The present Teeside Division of BSC includes Lackenby and Redcar on South Teeside, Consett and Hartlepool. Technical doubts have been expressed about the Redcar project now dependent on one very large (14 metre) blast furnace and at present without the necessary cover for relining, a lengthy process with a furnace of this size, which would be provided by a second furnace. The additional cost of a second furnace would be prohibitive in the present state of the market. Under existing arrangements it is intended to close Consett creating major employment and social problems in this single industry town. It is just possible that if Consett is separated off as a separate company a private sector partner might be found, but this seems improbable in the present state of the market. Clearly there is the basis for a single operating company based on Lackenby/Redcar although it is likely to need financial support for some time.

4. Sheffield Steel Company

The wide range of plants at Sheffield making stainless, alloy and carbon steels, forging and engineering products could be operated as a single company or as a number of separate companies. There is wide scope for private participation here either by 'hiving off' or through 'BP' type solutions.

5. The Scunthorpe Group

The particular attractions of this part of BSC's activities for private sector participation are the rod making plant at Shelton which could provide the basis for a rationalisation deal with GKN and the ore



terminal at Immingham which (combined with North Sea Natural gas) might provide the foundations for a private sector direct reduction plant. Though at present a lossmaker, the Scunthorpe Division, producing plates, sections and coiled rod, has a good labour relations record and with satisfactory management and private sector participation offers the prospect of a transformation into a successful and profitable company.

6. The Tubes Company

Those with considerable experience of the industry can see no reason why the production of steel tubes at Corby should not be profitable; and see this as a reformed semi Stewarts and Lloyds, possibly including Stanton and Staveley and the Midland tube operations. Once again this is seen as a unit suitable for a 'BP' type solution.

7. Shotton

Shotton could be included in the Steel Company of Wales or perhaps as part of one of the other finishing end companies or the steel holding company referred to below. A much better solution might be as an independent company; probably wholly or partly financed from the private sector, operating initially as a re-rolling company, buying in slabs for the hot strip mill, some from the competing state companies and some from abroad. The Hadfield's overture may just possibly offer a way forward for Shotton, retaining steel making; but if that does not come to anything, the buildings,

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plant and financial structure might be organised in such a way that at some more favourable time in the steel trade cycle part of its requirement for slabs could be met from its own steel plant based on electric arc furnaces.

There is plenty of scope for other permutations and this is no more than a first draft of a possible division of the present BSC. One possibility would be to group all the state owned steel interests outside the three main steel making areas under a single Steel Holding Company, which could be used as a staging post to increasing private sector participation. The important thing is to create a steel industry in which local management is given its head, each division can compete in the marketing of its own products and in which those employed can recognise that they will be rewarded for their efforts. In the present climate the biggest reward we can offer may be the possibility of survival; but I am certain as well that we should offer the workforce some way of sharing in the financial success of their companies. Sheerness provides a clear lesson and inspiration for us.

One risk of adopting my solution would be that individual companies instead of prospering in this competitive environment may fail. There are those that believe that far from offering the workers of Wales and the other plants a way out, we would be leading them to their destruction, weighed down by the

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burden of their capital debt and their outdated plant. But the alternative is a central plan, which may be wrong, based on a market assessment that almost certainly will be wrong and imposed by a top heavy central machine that will duplicate all the errors that have led us to our present condition. There will have to be a capital reconstruction that gives each company the possibility of survival and success; but if the companies then fail the consequences can hardly be more horrendous than those we face at present. I am firmly of the view that we will do better by far if we offer those involved a genuine chance of saving themselves by their own exertions.

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