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Dear Mike,

I enclose a short brief for the Prime Minister's use when, in company with my Secretary of State, she sees Sir Derek Ezra tomorrow.

We understand that the meeting is ostensibly a social one. However, it is too much to expect Sir Derek will not want to touch on his Board's current problems and to enlist the Prime Minister's sympathy for their proposed new approach. The Board's attitude has undoubtedly turned round - thanks to the pressure of our strategy on them - and is now very much along the lines we wish to see. For all that however, the Prime Minister will not, at this stage, wish to give a final view on the Board's proposals.

Sir Derek is also this year's Chairman of the Nationalised Industries Chairmen's Group. We have not, however, included material on current general nationalised industry problems for the sake of brevity. Should they be raised, the Prime Minister could refer to the continuing discussions between the Chancellor and the NICG.

Yours ever,

Geoff Darts

G S DART
Private Secretary



CONFIDENTIAL

MEETING WITH SIR DEREK EZRA: 28 JANUARY 1981

Brief for Prime Minister's use

Background

1. We understand that this meeting has been arranged at Ezra's request, and is primarily a courtesy call. However, it is likely that he may wish to touch on problems of coal policy, which are preoccupying the National Coal Board at the moment.

2. In Autumn 1979, Ministers agreed a financial strategy for the Coal Industry with three main parts:-

i. NCB should achieve break-even, without operating grants from 1983-84 onwards;

ii. over the period to 1982-83, operating grants would taper off. Upper limits on grants and EFLs for NCB were set as follows:-

	<u>£m 1978-79 Prices</u>			
	<u>1980-81</u>	<u>1981-82</u>	<u>1982-83</u>	<u>1983-84</u>
Total grants	192	166	85	57
EFL (including grants)	613	570	480	375

iii. social grants (basically assistance to men who lose their jobs when high-cost capacity is closed) to continue.

This strategy was based upon aims for productivity (OMS to increase 2% pa) and pit closures (1.5mt pa).

3. NCB have kept within their EFL for 1979-80 and hope to do so in 1980-81. Physically, the coal industry has performed well; absenteeism is at a record low level (12.3%); OMS has risen by about 1.5% pa (less than expected); high cost capacity has been eliminated at a rate in line with the Financial Strategy, and faster in 1980-81 (up to 3mt capacity).

Production is up (colliery output in 1980-81 is likely to be some 5mt higher than in 1978-79). However, because of the recession, coal demand has fallen sharply, and, for that reason, and because of high production, NCB expect to put 5mt more to stock this year than they had expected.



4. Looking ahead, NCB see no prospect of improvement in coal demand. They believe that it is now impossible for them to achieve break-even in 1983-84, or to keep within the EFLs which have been laid down. (They argue that cuts in capital expenditure, as well as endangering the longer-term future of the industry, would lead to short-term cancellation charges, and that drastic closures cannot be achieved without a substantial improvement in redundancy terms which they cannot finance from the money available to them.)

5. NCB therefore propose a new approach. They wish to eliminate their present "tail" of high-cost capacity as quickly as possible. In their judgement, they cannot go faster than eliminating 17-18mt of high-cost capacity by 1985-86, and to do so they will need a substantial improvement in redundancy terms. Even so, the risk of industrial relations trouble is obvious. In addition, the Board plan to achieve continuing increases in output and productivity at long-life collieries, and to maintain tight financial control, so that unit operating costs increase by no more than general inflation. (This will involve, inter alia, keeping labour costs, at worst, constant in real terms).

6. At the same time, the Board want to maintain capital investment at a level which would allow continued creation of low-cost capacity. (They argue that not only will this output be needed in the longer-term, but that continued investment will make it easier for the miners to accept closures).

7. To achieve these aims the Board seek Government help in:-

i. covering the additional "social costs" of pit closures;

ii. safeguarding sales of 120mt pa of coal over the period to 1985-86. (This would mean phasing out present coal imports, except where needed on quality grounds, and some financial assistance to encourage industry to convert from oil-fired to coal-fired boilers);

iii. devising financial arrangements to assist the Board to bear the cost of holding substantial cost of coal;

iv. an increase in the proportion of grants within the EFL to give the Board a prospect of breaking even each year.

On this basis, the Board argue that they will be able to bring a capacity into line with demand by 1985-86. The Board should then be financially viable.



8. The Board are to meet the National Executives of the three mining unions on 10 February, to explain the Board's plans for dealing with the industry's financial problem. These centre on increased closures. The Secretary of State has told Ezra that the Government cannot reach a final decision by 10 February. Ezra accepts this.

9. So far neither the Secretary of State for Energy nor Ministers collectively have considered the Board's proposals. The Secretary of State has, however, told Ezra that it must remain the Board's responsibility to keep a proper balance between supply and demand and that the Government is unlikely to agree to take action to maintain demand at artificially high levels, and that he agrees with the need for substantial closures of uneconomic capacity. He believes that there is a strong case, as the Board suggest, for improved redundancy terms and for helping the Board to finance the other additional costs imposed by a higher rate of closure. The Secretary of State intends to put his proposals to colleagues in due course.

10. Ezra has also repeatedly pressed the idea of some sort of presentation by the Board to the Secretary of State and his colleagues. The Secretary of State has not yet accepted this idea and would, in any case, wish to consider its timing.

Suggested Line

11. The Prime Minister will not wish to initiate a discussion of the Board's proposals, unless Ezra raises the subject.

12. If he does so, she might make some or all of the following points:-

i. she recognises the efforts which the Board have made to keep within the present Financial Strategy;

ii. she recognises too the courage that is involved in grasping the nettle of closures.

iii. she has not yet, however, discussed policy for the coal industry with the Secretary of State and her other colleagues, and would not want to discuss the substance with Sir Derek until she has done so;

iv. she does not believe that it will be possible to give any firm Government view before 10 February.