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10 DOWNING STREET

THE PRIME MINISTER

13 May 1983

Handwritten signature: Ian Stewart

Thank you for your letter of 5 May about the prospects for the UK shipbuilding industry.

I am, of course, well aware of the widespread concern both inside and outside the industry and the very difficult problems it is currently facing. But the fact is that the demand for new merchant ships has fallen dramatically during the world recession - and is unlikely to pick up markedly for some time to come. At the same time there has been a decline in orders for oil rigs as a result of the reduced demand that has followed the second major oil price rise of 1979. The deterioration in the market is posing severe problems for virtually the whole of the European industry and even for the Japanese.

It is quite wrong to imply that the Government have in any sense abandoned UK shipbuilding in the face of these problems. On the contrary, we have provided extensive support - £700 million for British Shipbuilders (BS) alone since 1979. In the forthcoming year we have made provision for £90 million of capital expenditure by BS - over four times the level we inherited from the previous administration.

Although BS' order book is short at some yards, they have recently taken important orders for merchant ships from Ethiopia and Mexico which will provide 640 man years of work for Austin and Pickersgill and 2,400 man years for Sunderland, and more orders are in the pipeline. There have also been the recent announcements by Ian Stewart on 10 and 12 May about the procurement of further naval ships.

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I should also remind you of the Government's record on orders for the Royal Navy. Since we came into office in May 1979, we have ordered 23 warships from BS yards worth over £1,830m. We have also recently announced our intention to procure a further nuclear powered fleet submarine, two further frigates, and the first of a new class of patrol submarine; in addition we are now offering Clelands, a BS yard, the opportunity to build two Fleet minesweepers under the Development Area Preference Scheme. The total value of these further ships is nearly £600m..

Despite the orders that BS have signed, or have in prospect, this is a difficult situation for them. You will know that the Chairman, Sir Robert Atkinson, has recently asked us to consider further support to tide BS over the shipbuilding recession and to help them obtain orders in the current climate of strong competition from the Far East. We are considering these proposals carefully. It is however important that decisions on this should not be made on short term considerations but on the basis of a considered view of BS' overall business prospects, which BS is currently preparing.

We recognise, however, that in the intervening period there may be a need to help BS receive more orders. Patrick Jenkin made it clear in a written Parliamentary Answer on 12 May, that he has told Sir Robert that we are prepared to give careful consideration to specific requests for help to obtain orders on a case-by-case basis. This will have of course to be within the framework of our international obligations.

I think you will agree that the specific proposals you make will best be considered alongside our examination of Sir Robert Atkinson's. But I can make some initial comments:-

(i) an accelerated building programme would mean building ships before they are needed and this would be bound to involve a financial penalty and thus an addition to the sums Government already spends to support British Shipbuilders. It is far from clear that this would be cost effective.

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(ii) the UK, like most shipbuilding nations, including Japan, is a party to the OECD Understanding on export credit for ships, which sets a framework for credit terms on export orders. A departure from these terms would encourage others to follow suit and risk starting a subsidy race. In any case where others offer better terms than the Understanding permits the Government is prepared to match these terms where this would be appropriate.

(iii) we are exploring with British shipowners the possibility of improving the terms of the Home Credit Scheme. Although Japan's Home Credit Scheme is more favourable than ours, Japanese shipbuilders, unlike those in the UK, do not receive production aids such as our Intervention Fund;

(iv) most public sector orders for ships are in fact already placed in UK yards. But it would be quite wrong for the Government to seek to compel public sector purchasers to order in the UK regardless of commercial realities.

(v) you refer to advance orders for oil rigs placed under a previous Labour Government. I would point out that market conditions have changed markedly over the years and that there are currently large surpluses in almost every type of oil rig. In these circumstances there would be a large risk that any rig ordered speculatively would not find a market for a considerable time to come. I am not prepared to risk the taxpayers' money in this way.

When Patrick Jenkin met the leaders of the "Save Our Shipyards" campaign in Newcastle last Friday, he discussed these issues with them and made one further point which I would like to put to you. It is that further support for BS has to be paid for by the rest of the country. In particular, the cost is in effect carried by firms who are competitive, such as NEI-Parsons Limited

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which has recently won a major order in Singapore for power generating equipment in the teeth of international competition and against the background that Japan had gained virtually every order in Singapore for this type of equipment since 1963. If a firm like NEI-Parsons can compete with the Japanese and beat them, why cannot BS? The fact is that NEI-Parsons has raised its productivity sharply over the last few years while at BS productivity is still not back to the pre-nationalisation level and is estimated by BS to be 2½ times worse than Japanese ship-building productivity. There must be some limit to the burden which it would be right for the Government to impose on successful competing firms in order to support those who over the years have shown themselves unable to compete.

I have every sympathy with the difficulties facing shipyard workers, but against the background of facts like these part of the solution at least rests in their own hands. The Government is perfectly prepared to play its part as we have done over the last four years. You invite me to make a commitment to the future of the industry. In fact this commitment is already manifest in our strong record of support. As I have made clear we have provided a very great deal of support since 1979. This must be matched by corresponding determination to be competitive on the part of management and workforce.

The Government's policies are designed to help BS achieve viability. This means, as I have said, that further support must and will be linked to the long-term business plans of the Corporation. But, equally important, it means that there must be a whole-hearted commitment to the future by the management and the workforce of British Shipbuilders. Their losses for 1982/83 are likely to be considerably higher than last year, but this deterioration is not caused by a lack of orders but by losses they will have incurred on orders already obtained.

The current threat by the Unions to occupy the yards in protest against any further restructuring which may prove necessary is the worst possible way in which to help overcome these problems

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or to secure the future of the industry. The only effect of a sit-in would be to damage yards further. I very much hope you will use your efforts to persuade them against this.

Yours sincerely
Raymond Deakin

The Rt. Hon. Michael Foot, M.P.