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MR WALTERS O/R

cc Mr Mount
Mr Scholar

PIT CLOSURES

I have been sent, on a personal basis, the attached NCB draft of their financial projections to 1992/93, which is in effect the Board's discussion document on pit closures. I have undertaken that we will not trouble the Prime Minister with it at this stage, and will use it only to prepare ourselves for the official and, ultimately, Ministerial discussions which will begin in mid-January on the basis of a final version. I should be grateful if you and Ferdie would have a look at it and let me have your reactions (I am sparing Ferdie the rather bulky Annexes, except for the crucial Annex F); and I am sending a copy of this note to Michael Scholar to keep him abreast of what will be a major issue in the New Year (he will recall that Mr Lawson referred to the existence of the draft in his note of 10 December to the Prime Minister).

The NCB and, frankly, to some extent Ministers also, see pit closures chiefly in the context of industrial action, threatened or real. That is one perspective. But there are others. I think a better starting point for this debate is to remind ourselves of the wider context:

(i) It is absolutely fundamental to the Government's strategy to reduce the burden of the loss making state enterprises. The principal loss makers are the constituents of the triple alliance - coal, steel and rail. BSC has survived, with its five main centres of production, in the face of all economic logic, for political reasons. BR is on a shakier political base, but we shall do well to keep open the possibility of substantial network reductions until after the election. Can the Government retain the credibility of the strategy if it shrinks from substantial reductions in unwanted coal production?

(ii) And there is already a very specific Government objective for coal, born out of the CPRS study of relations with nationalised industries, to which we were midwife. On 18 June 1982 Mr Lawson circulated to his colleagues the text of the objectives he had agreed with Mr Siddall. The second paragraph reads as follows:

> "The NCB should aim at that share of the market, which they can profitably sustain in competition with other fuels, including imported coal. The Board should not plan on any continuing tranche of sales which will not be profitable. The Board should bring its productive capacity into line with its continuing share of the market."

Seen in this context, the NCB's discussion document is a poor relation of the firm policy on closures we expected from Mr Siddall in the aftermath of his victory over Scargill on pay. It is also difficult to follow; but we must make allowances for its being only a draft.

The opening passage on the Board's Objectives sets the tone for the rest. They are muddled, and difficult from the objectives set by Mr Lawson. The Board then offer two illustrative strategies, "rapid" and "conventional". The difference between the two is about 6% less deep mined coal production by 1986/87, achieved by a faster rate of closures. The Board assume that adoption of the rapid strategy would be accompanied by a 4-week national coal strike, and the conventional strategy by some local action. Neither strategy relates output to demand at all clearly, and there is no consideration of the relative cost of imported coal. It could not be argued that either strategy brings the Board's capacity into line with its continuing share of the market. Nonetheless, the Board's recommendation, accompanied by dire warnings of impending industrial relations problems, is that they adopt the conventional strategy.

The financial consequences of the two strategies are hard to disentangle from the paper. Under the conventional strategy, the EFL falls to zero by 1989/90, with coal being sold at a profit somewhat before then (as we already know, the greatest losses can be most easily saved because they are concentrated in a few pits). Figures for the rapid strategy are not shown on the same basis.

The recipients of this note may well be struck by the similarities with the Serpell report: a weak analytical starting point, uncertain financial projections, a radical strategy dismissed as impracticable, a comfortable strategy embraced as being consistent with the achievement of breakeven by the end of the decade.

So the issues on which we need to reach a judgement are these:

1. How do the levels of production in the two strategies relate to the level of demand, and the relative price of imports?

2. What are the precise financial consequences that the Board foresees for its two strategies?

3. How likely are they to be achieved?

4. At what rate of pit closures does the threat of localised resistance become a threat of a national coal strike?

J.

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