CONFIDENTIAL

THIS DOCUMENT IS THE PROPERTY OF HER BRITANNIC MAJESTY'S GOVERNMENT

C(85) 3 COPY NO 79

22 January 1985

CABINET

THE ORDER FOR TYPE 22 FRIGATES 13 AND 14

Note by the Secretary of State for Trade and Industry

I made clear in my minute of 21 December 1984 on this subject in reply to the Secretary of State for Defence's minute of 18 December that his proposal that the orders for the two Type 22 frigates should be split between Cammell Laird and Swan Hunter instead of both being placed with Swan Hunter needed very careful consideration in the light of the wider implications of our decision.

2. The attached note which has been agreed between officials in my Department, the Treasury and the No 10 Policy Unit brings out clearly the principal financial and employment effects of our decision. In broad terms the effect of saving 1,200 jobs at Cammell Laird will be to cause up to 1,200 extra redundancies over time at Swan Hunter at a cost to the Ministry of Defence of some £7 million, and at an additional cost to British Shipbuilders possibly of the order of £40 million or more.

N T

Department of Trade and Industry

22 January 1985

CONFIDENTIAL

THE ORDER FOR TYPE 22 FRIGATES 13 AND 14

NOTE BY OFFICIALS

Introduction

1 The purpose of this note is to provide factual background and forecasts bearing on the allocation of the orders for Type 22 frigates 13 and 14. It has been agreed between officials of HM Treasury, DTI and the No 10 Policy Unit. For the most part it concentrates on a comparison of the effect of:

Course (a) placing both orders with Swan Hunter; and

Course (b) splitting the orders between Cammell Laird and Swan Hunter.

Direct Costs

2 In accordance with Cabinet's decision on 19 July 1984, the Ministry of Defence sought fresh tenders for the two ships from Cammell Laird, Swan Hunter, and Vosper Thornycroft. Tenders were returned on 15 September. Swan Hunter and Vosper Thornycroft bid for an order for both ships or either one of them. Cammell Laird tendered for one or other ship but not both. The results of the tendering process may be summarised as follows:

JH1BTU

	£m	
2 ships from Swan Hunter	139.4	Course (a)
2 ships from Vosper Thornycroft	140.9	
1 ship from Vosper Thorneycroft and 1 from Swan Hunter	145.2	
1 ship from Cammell Laird and 1 from Swan Hunter	145.5	Course (b)
1 ship from Cammell Laird and 1 from Vosper Thorneycroft	147.2	

In addition, MOD would incur extra costs of about £1m if the order were split. The total extra direct costs of course (b) over course (a) are thus about £7M.

Indirect Costs

3 When considering indirect costs and redundancies, assumptions need to be made about the level of other work and the allocation of overheads. In providing figures therefore, BS have assumed the same allocation of overheads as was used in the tenders submitted to MOD. Under course (a), unless special action were taken (see para 9 below), BS would close Cammell Laird within two or three months. They would propose to move HMS Edinburgh to another ship-or dock-yard for final fitting out. Under course (b) there would probably be an under-recovery of overheads at Cammell Laird, of some £10m over 1985/6 and 1986/7 together; BS expect Swan Hunter to incur extra under-recovered overheads of £5M in 1985/6 and 1986/7 together with higher figures in later years.

JH1BTU

Redundancies

4 In February, Swan Hunter will employ 5,200 after the current round of 2,100 redundancies is completed. Cammell Laird currently employ 1,700 after implementing 1,600 redundancies in 1984. Both yards are likely to have to declare a further 500 redundancies in 1985 whatever course is chosen.

The yard that does not win the second order will have to declare some 1,200 further redundancies, resulting in Cammell Laird's case in closure. The cost of the 1,200 redundancies will be some £6½M under the Shipbuilding Redundancy Payment Scheme (SRPS).

Unemployment

5 Three of the four Swan Hunter yards are in the Newcastle travel to work area (TTWA). Cammell Laird is in tne Wirrall and Chester TTWA. Unemployment rates are as follows:

	Average of 12 months to December 1984	December 84
Wirral and Chester	17.9%	18.2%
Newcastle	17.9%	18.0%

Unemployment rates in the adjacent TTWAs are as follows (1 Swan Hunter yard is in the South Tyneside TTWA):

Liverpool	20.6%
South Tyneside	24.5%

JH1BTU

Industrial Relations

6 In recent years there has been considerable industrial disruption at Cammell Laird. The percentage of man hours lost due to strikes and stoppages at Cammell Laird has been above the BS average. CL has lost over 1.3% of possible man hours each year since 1981/2. It lost nearly 4% in 1983/4. The comparable figures for Swan Hunter have never risen above 0.4%. In July 1984 the Cammell Laird workforce were laid off as a result of industrial action over compulsory redundancies and some of them occupied the work in the yard. 37 sitters-in were jailed in October. As a result of an unofficial Back to Work Committee the workforce on 9 November unanimously rejected a strike call, and over 90% of them are currently at work. At Swan Hunter, the workforce have accepted the current round of redundancies without industrial action and against union advice. Although the "strike" at Cammell Laird remains official, the national union conference (SNC) recently made a low key request to the Minister of State for Industry (Mr Lamont) for a Type 22 frigate order to be placed with Cammell Laird. Both yards have agreed to implement the British Shipbuilders Phase V wage agreement incorporating new working practices.

Overcapacity

7 As demonstrated in the annex, the current capacity in the UK to build large surface warships is seven to eight frigate equivalents a year against an anticipated MOD requirement for four (three frigates and one large auxiliary). The only immediate export prospect is two frigates for Pakistan which Vosper Thornycroft hope to win. MOD will need a second submarine line at a maximum order rate of one frigate equivalent. If Yarrow or Cammell Laird were

JH1BTU

to win the submarine order and Vosper Thornycroft to win the Pakistan order, the available capacity for surface ships would fall to about six to seven frigate equivalents against MOD requirements for four. If Cammell Laird were to close and be sold as a facility, the capacity immediately available would fall on the same basis to four to five frigate equivalents, thus largely eliminating the overcapacity. It would be possible however for the new owners of Cammell Laird to attempt to re-enter the warship market.

Privatisation

8 Under course (a), BS estimate the closure costs to them (ie excluding SRPS) of Cammell Laird would be some £10M; they would then expect to sell Cammell Laird as a facility for a few million pounds. The net costs would be of the order of £5m. Under course (b), Cammell Laird would continue in existence at least for the four years required to build the frigate. Even so, because of the anticipated level of losses, and the need for further investment, BS and Lazards believe that it could only be privatised if privatisation were accompanied by a cash injection of the order of £20m at least. Course (b) reduces Swan Hunter's profits by some £20m over the period with a comparable effect on privatisation proceeds.

Special Action for Cammell Laird

9 BS have considered in conjunction with Lazards whether special action at Cammell Laird would improve the position under either course. In particular, they have considered the effect of an award to Cammell Laird on a non-competitive basis of a contract for the conversion of the Balder London which would provide a certain work load for about one year.

JH1BTU

It could increase MOD's costs by some £2-3m. Under course (a) in BS's view, the award of a Balder London contract would be insufficient to prevent closure of Cammell Laird. However, if a further MOD contract of a similar size to the Balder London conversion were awarded to Cammell Laird, BS believe that they may be able to sell the yard to someone in the offshore sector preserving at least temporarily up to about 700 jobs. But there can be no certainty that this would provide a future for Cammell Laird and MOD have been unable to identify a suitable potential contract. The costs of such action seem certain to exceed the costs of closure and disposal. Under course (b) the award of a contract for the Balder London would marginally improve the position of Cammell Laird and would defer some 300 redundancies. It would not however make the yard viable and it would only be sold with a very considerable dowry.

Summary comparison of effects of main alternatives

	COURSE (A) (both Frigates at Swan Hunter)	COURSE (B) (one Frigate at Swan Hunter; one at Cammell Laird)
1 Direct Costs	-	Extra costs of £7m to MOD
2 Indirect Costs	-	Extra losses of some £1.5m at Swan Hunter and £5m at Cammell Laird in 1985/6. Effects in later years affect privatisation proceeds.

JH1BTU

3	Redundancies	1,200 at Cammell Laird*	1,200 at Swan Hunter*
4	Privatisation	Closure of Cammell Laird and sale as a net cost of some £5m.	Reduction of Privatisation Proceeds at Swan Hunter of some £20m. Cash injection into Cammell Laird of at least £20m.

16.1.85

* In addition both yards are likely to have to declare a further 500 redundancies in 1985

JH1BTU

ANNEX

WARSHIPBUILDING CAPACITY

(excluding submarine building at Vickers)

UK Capacity from 1986 (a)	**Minimum Capacity**	**Maximum Possible Capacity**
Cammell Laird (b)	1.5	2
Swan Hunter	2.5	2.5
Vosper Thornycroft	0.5	0.5
Yarrow (c)	1.5	2.0
Harland & Wolff (AOR only)	1.0	1.0
	7.0	8.0

Demand (a)

Orders pa
(average of 1985 - 1990)

Frigates	3	3
AORs	1	1
	4	4

Further demand might be generated from exports, refits, merchant work and second stream submarine building.

Notes

(a) 1 AOR build time approx = 1 Frigate
(b) 2 now, decreasing to 1.5 if yard restructured
(c) 1.5 now, increasing to 2 if module hall built.

DTI
15 JANUARY 1985

4