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P 01821

PRIME MINISTER

WESTLANDS
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BACKGROUND

1. Westlands current turnover is £300 million a year, and the company employs 12,000 people (7,500 of them at Yeovil). By far its most important customer is the Ministry of Defence; the most significant civil application of helicopters is the servicing of offshore oil and gas installations. There are 4 major European helicopter manufacturers; Westlands, Agusta (Italy), Aerospatiale (France) and MBB (Germany); it seems unlikely that the market will prove sufficient to support the maintenance of the full range of design, development and production capacity at all of them.

2. There are three basic types of helicopter - large, medium and small:

(a) Large - Westlands are jointly developing with Agusta the EH 101, for both civil and military applications. Production is due to start about 1990.

(b) Medium - the 4 European countries are conducting a feasibility study for the collaborative development of the NH 90. The Sikorsky Blackhawk is in the same range, as is the Aerospatiale Super Puma and the improved version of the Westland W 30 (for which Westlands have received £40 million DTI launch aid). The Ministry of Defence position is that they do not propose to buy Blackhawk, Super Puma or W 30, but will instead make do with existing Wessexes and Sea Kings until the NH 90 is available some

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time after 1990. Helicopters in this range have some civil as well as military potential.

(c) Small - at present there are two competing European approaches to the development of a new battlefield helicopter: one involving Aerospatiale and MBB, and the other Westlands and Augusta (on the basis of a new version of the Agusta A 129).

3. Westlands have been losing money, and unless a financial reconstruction is in place by the time the company's accounts for the year to 30 September 1985 are published on 19 December, the company will go into receivership. There have already been major management changes, with the appointment of Sir John Cuckney as Chairman. New equity money is needed, as well as the conversion of some bank borrowing into equity, and a rights issue. Two proposals have been made:

(i) Sikorsky, in association with Fiat, would put in up to £30 million, and would take a stake of up to 35-40 per cent in the company. Westlands would be given a licence to manufacture the Sikorsky Blackhawk for sale in European and certain other markets;

(ii) Aerospatiale, MBB and Agusta would put in at least £25 million and possibly up to £40 million in return for a 30 per cent stake. (The offer is firm from Aerospatiale and MBB, but the participation of Agusta is conditional on the Italian Government who have not yet taken a clear position.) British Aerospace may also offer to take some share in a European support operation; their Board are discussing the issue this morning, and a report may be made to the meeting.

4. Meanwhile the National Armaments Directors (NADs) of the four countries have recommended to their Governments that all their requirements for helicopters in the three categories

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above should be satisfied by equipment designed and built in Europe. The implication of this would be that the NH 90 would go ahead; the two competing battlefield projects would be amalgamated; and Aerospatiale and MBB would take a stake in the EH 101. If the Government endorsed this recommendation, it would rule out the purchase by MOD of any Sikorsky - designed helicopter built by Westlands; the company accordingly take the view that they cannot go ahead with a Sikorsky - backed financial reconstruction unless the Government make clear that they do not intend to endorse the NADs' recommendation.

Advantage and disadvantages of the two proposals

5. The Secretary of State for Trade and Industry considers that it is essentially for Westlands to make a commercial decision between the alternative reconstruction arrangements. Westlands (whose Wessex and Sea King are basically Sikorsky designs) believe that the Sikorsky option gives them better prospects of getting through the next few years when UK military orders will be scarce, essentially through export sales of Blackhawk. They also consider that they can gain more from Sikorsky in terms of management strength and design capability, as well as long-term stability for the business. Meanwhile the European option offers relatively little in assured new work - some subcontract assembly work for Aerospatiale, the possibility of manufacturing the A 129 under licence if additional orders can be secured, and the possibility of participation in the development of further versions of the Super Puma. (There is some suggestion that Westlands might also secure some further subcontract work on the Super Puma, of the order of £10 million or so, in return for UK use of Ariane rather than the US Shuttle, but there would be some cost to MOD, again of the order of £10 million. But the main beneficiary of further Super Puma orders would, of course, be Aerospatiale.)

6. The Secretary of State for Defence strongly prefers the European option. He argues that the Sikorsky option would mean

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- (i) exclusion of the UK from European collaborative projects;
- (ii) leakage of UK/European technology to the US;
- (iii) because of the adverse German reaction, risks to EFA;
- (iv) the progressive weakening of the European helicopter industry, with a major element falling under US control.

On the other hand the European option would promise better prospects in the long run, because of the wide market promised (from the mid-1990s) for the products of the collaborative developments now under way or in prospect. Meanwhile MOD argue that that that the greater economy of developing the new battlefield helicopter on a quadripartite basis would save £25 million which could be spent on addition orders for presently available Westland helicopters (although no explanation is offered why it would be right to purchase these aircraft which, on present plans MOD were intending to do without).

MAIN ISSUES

7. The joint paper by MOD and DTI officials identifies three issues on which Ministers need to reach views:

- (i) is it acceptable for a major defence contractor to come under effective foreign (i.e. US) control?
- (ii) What position should the Government take on the recommendation of the NADs?
- (iii) What should be done about the £40 million launch aid already given to the Westlands W 30-300?

Sir John Cuckney will be in attendance at the meeting of the Sub-Committee; in order to inform Ministers decisions on those issues which are a matter for Government, he might be asked to comment on:

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- (a) the financial implications of the alternative courses for Westlands in the immediate future;
- (b) the impact of the alternative courses for Westlands' management and design/development capability;
- (c) Westlands' view of the implications of the alternatives for the future of the EH 101 and NH 90 projects, and also the future rationalisation of the competing battlefield helicopter projects;
- (d) the prospective loading on Westlands' manufacturing facilities of the alternative arrangements, given that MOD will not buy either Blackhawk or any version of the Super Puma.

An independent UK capability

8. As already noted, Westlands have had a long-standing relationship with Sikorsky on helicopter design and development. As is now apparent, the management of the company have not been successful in establishing a UK operation which can stand on its own in the world market. Either option appears to involve some reduction in the extent of the UK independent capability; in the case of Sikorsky, there would be significant dependence on US design capability and management expertise, while in the European case Westlands would be dependent in the short run on sub-contract work for Aerospatiale (or Agusta), and in the medium term would be wholly dependent on the collaborative development projects. It is not clear that an independent UK capability to develop helicopters is fundamental to this country's security; if it is considered acceptable for Westlands to become partially dependent on foreign companies, whether US or European, there can only be a choice if it is clear that neither course poses fundamental risks to Westlands' survival. The first question then would be whether the uncertain prospect of sub-contract work, etc in the case of the European option would be sufficient, with the

The Defence Secretary did not think so earlier this year, when the MOD were asked to chip in to help Westland afloat.

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proposed cash injection, to keep Westlands going until the collaborative projects come to fruition after 1990. If not, the further questions become academic.

The NADs' recommendation

9. From the standpoint of European collaboration, the recommendation has obvious advantages. But it would mean the elimination of any element of competition from the European military helicopter market. On the other hand rejection of the recommendation is argued to prejudice the prospect of the UK participating on the NH 90 and the battlefield helicopter projects (and perhaps also to put at risk the EH 101). It is argued in particular that the Sikorsky link means the transfer of UK technology to the US, and that the other European manufacturers would be unwilling to have Westlands as their partner on this account: but it is doubtful whether the technological capability of the UK and European industries is of great interest to the US. So far as Agusta is concerned, Westlands' participation in the EH 101 is essential to the future of the company; this suggests that Agusta's support for the European option might not be maintained if it appeared that this would not be sufficient to save Westlands from receivership. In practice, on the information available, it does not appear that the Sikorsky link necessarily means the failure of the EH 101 project; and the European option undoubtedly involves some dilution of Westlands' interest in it. Nor is it clear that the battlefield helicopter could not go ahead as a 4-country collaboration in the event of the Sikorsky link, although clear arrangements would no doubt be needed to safeguard the ownership of the technology. UK participation in the NH 90 would be more at risk because of competition with the Blackhawk; but the question then arises whether there is any real need to develop a European rival to this type of aircraft.

Launch aid

10. DTI and the Treasury are agreed that, whichever option is followed, the Government should make clear that no attempt will be made, in the event of the W 30-300 being discontinued, to

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recover the £40 million launch aid given to the project except in the event of liquidation of the company. It would seem sensible for Ministers to endorse this collectively, thus avoiding the need for damaging qualification of Westlands' accounts.

Westland's own views

11. It will be necessary to establish Westlands' views on the alternative possibilities, and in particular on the questions set out in paragraph 7 above.

HANDLING

12. I suggest that you handle the meeting in the following stages:-

(i) explore first the prior question of the importance to be attached to the maintenance of an independent UK design and development capability for helicopters, and the prospects of securing this on the basis of either option for the future of Westlands. The Secretary of State for Trade and Industry and the Secretary of State for Defence will wish to state their positions. The Chief Secretary, Treasury will wish to comment on the public expenditure implications which could be very substantial if the Sikorsky link were ruled out and the European option proved insufficient by itself to avoid receivership (keeping Westlands alive could then involve large continuing Government subsidies). Other Ministers may wish to comment on the employment and political implications;

(ii) then invite Sir John Cuckney to join the discussion, so that he can make clear the company's view point, and answer any questions, in particular on the financial implications of the options and the other main points suggested in paragraph 7 above;

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(iii) finally, after Sir John Cuckney has left the meeting, the Sub-Committee will need to reach conclusions on the outstanding matters for the Government listed in paragraph 13 below. It may be suggested that decisions should be delayed to give time to secure further participation in (ie by British Aerospace) and further advantages from (ie Super Puma sub-contract work) the European option. Two more days delay might just be tolerable; but you would need to be satisfied that there was a real prospect of securing additional long-term advantages from such proposals rather than simply minor palliatives.

CONCLUSIONS

13. You will wish to reach conclusions on:

(i) The importance of maintaining a UK helicopter design and development capability independent of the US, and the additional public expenditure costs it would be right to incur in order to achieve this (the key question is which option offers the better prospect for Westlands' immediate survival and longer term success);

(ii) the Government's response to the recommendation of the NADs: acceptance of the recommendation would preclude the Sikorsky option;

(iii) the question of the repayment of the W 30-300 launch aid.



J B UNWIN

Cabinet Office
11 December 1985