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From the
Minister of State
PS/Norman Tebbit MP

Mike Pattison Esq
Private Secretary to the
Prime Minister
10 Downing Street
Whitehall

Prime Minister
You asked about the
level of subsidy
involved here.
4 June 1981

MS

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2. Pa

MAP 4/v1

MAP 7/v1

Den Mith

CAMELL LAIRD: DOME PETROLEUM

I attach as requested a copy of the letter circulated to E(EA) setting out the background to this order. Treasury agreement was given on 12 May. I should add that due to subsequent movements in the exchange rate it now looks as if the loss incurred by British Shipbuilders could be as low as \$3-4 million compared with the maximum of \$8 million approved by the Treasury. This represents the extent of the Government subsidy to this order and will be contained within the loss limits of British Shipbuilders.

Yours sincerely
Peter Mason

PETER MASON
Private Secretary

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Shipbuilders
Orders

DEPARTMENT OF INDUSTRY
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From the
 Minister of State
 Norman Tebbit M

Rt Hon Leon Brittan QC MP
 Chief Secretary
 HM Treasury
 Whitehall

8 May 1981

Dear Chief Secretary.

CAMMELL LAIRD: DOME PETROLEUM

I am writing to seek your agreement that British Shipbuilders should offer limited financial concessions outside the normal financial arrangements (involving BS in some loss) in order that Cammell Laird may secure an order from Dome Petroleum of Canada for a semi-submersible drilling rig. I should normally expect to bring these proposals to E(EA) but, because Dome are anxious to reach a very early agreement with BS, it is necessary that I should seek your agreement in correspondence.

During detailed negotiations with Dome the competition for this order has been reduced to a straight battle between Cammell Laird and an experienced Swedish yard, Gotaverken. Dome have expressed themselves totally satisfied with the facilities at Cammell Laird and the ability of the yard to complete the contract. My officials have examined the basis of the cost estimates prepared by the yard and believe that they are realistic, not least because they have been compiled on the basis of detailed advice from Highland Fabricators, an experienced private sector offshore yard. There nevertheless remains a price disadvantage to Dome from a UK build. The total cost to Dome of the Cammell Laird is \$145.3 million (at £1 = \$2.27) whereas the Swedish offer on a comparable basis is \$128.4 million. Dome have stated that they are prepared to meet \$5 million of the gap of \$16.9 million in order to build in the UK.

The rig does not qualify for Intervention Fund support. However, the rig will be owned by a UK registered company and will therefore qualify for normal Home Credit Scheme support for rigs (~~85% of contract price at 8 1/2% over 8 1/2 years from delivery~~). Some reduction of the gap can be achieved by detailed adjustments to the credit arrangements within the overall terms, which do not conflict with our international obligations or our agreed procedures for operating the Scheme. These save about \$2 million. The residual gap, after allowing for Dome's contribution, therefore reduces to \$8.9 million.



Dome have suggested that all but \$2 million of this gap can be eliminated if the contract is struck in dollars at a fixed rate of £1 = \$2.135. (The original comparison being based on £1 = \$2.27.) This would be accompanied by a dollar loan under the Home Credit Scheme. British Shipbuilders frequently enter into dollar contracts for the sale of ships and seek to protect themselves by forward sales of the dollar receipts. However, in the current state of the currency markets, BS could not achieve forward sales at a level which would avoid all currency losses on the transaction. On the basis of current forward rates extending up to delivery in June 1983, BS would suffer a currency loss of up to \$6 million.

BS propose to meet the remaining \$2 million by offering to pay some or all of the building supervision costs which will be incurred by Dome. These are estimated to total some \$3 million so there is some scope for offering Dome a trade-off between these and the actual exchange rate at which the contract is struck. For example, meeting all of the \$3 million supervision costs could enable the contract to be struck at £1 = \$2.155.

In any event, the potential loss to BS on this contract is \$8 million, equivalent to £3½ million. BS have confirmed that this sum can be met within their existing loss limit.

When we considered the KCA case in E(EA), I emphasised the critical importance of an early offshore order for Cammell Laird, particularly in the context of the cutback in Naval ordering. Whilst BS are still negotiating with KCA, it is still likely to be some while before a contract can be placed and meanwhile Cammell Laird are approaching the point in time when there will be severe underutilization at the yard. The yard is currently forecasting a profit of about £2½ million on naval work in the current year if an early offshore order is secured, but this prospect will otherwise be rapidly eroded due to underutilization. Dome are anxious to place their order very quickly. Their President, Bill Richards, will be in the UK at the end of next week and hopes that a final decision can be reached by then. (He is due to meet Hamish Gray on Thursday.)

You will be anxious to know how this order fits in to the future of Cammell Laird and Scott Lithgow given the likely reduction in MOD work. Until BS have produced their Corporate Plan and it has been modified in the light of the defence review and agreed with Government, it is impossible to predict the prospects for these yards nor, indeed, those of many other yards in BS. No guarantee can, therefore, be given that either Scott Lithgow or Cammell Laird can survive but at this stage it seems to be reasonable to assume that it may well be possible for one or the other of them to do so primarily on oil related work. Unless, however, we wish to precipitate an early crisis by default at Cammell Laird, it would be desirable to



authorise BS to take this order which would also give Cammell Laird experience of rig work and aid their prospects of competing in offshore. Moreover, Keith Speed has already made the point in relation to the KCA case that taking an offshore order would help ease any problems involved in completing existing defence contracts at Cammell Laird which I fear would otherwise go sadly awry. I should also add that should KCA place an order for a rig, Cammell Laird could build it as well as the Dome order, though some of the work would have to be sub-contracted, probably to Scott Lithgow who also need a rig order soon to avoid underutilization in the autumn.

I believe that Cammell Laird have done extremely well to come so close to matching the competition on normal commercial terms. By way of comparison, the direct subsidy level being sought to close the remaining gap is less than 6% compared with the 23% normally necessary to secure merchant ship-building orders. The winning of a major offshore order from a foreign oil company would be a real boost to the yard's prospects of establishing itself as a credible force in the offshore market.

I should therefore welcome your urgent agreement that BS should offer: ..

i a fixed dollar contract at a rate of not less than \$2.135 = £1; and

ii to meet that proportion of Dome's supervision costs necessary to bridge the remaining gap.

I should require BS to limit their foreseen loss to \$8 million (subject to the actual forward rates at the time of agreement) and to negotiate a deal which served their best commercial interests. I am sorry to press for such a speedy response, but we only received Dome's proposals this week and they are anxious to reach agreement before Mr Richard's visit next week.

I am copying this to colleagues in E(EA).

Yours sincerely
PE Munn

pp NORMAN TEBBIT