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Prime Minister (2)  
To note



FROM: THE CHIEF SECRETARY  
DATE: 31 January 1984

PRIME MINISTER

cc E(A) Members

LAUNCH AID FOR THE A 320

We are to discuss Norman Tebbit's proposal to give launch aid for the A 320 on Thursday at E(A). To do so Norman suggests would be inconsistent with our general policy and I thought that I should put on record that I am opposed to providing any assistance.

The plain truth is that the A 320 on the most likely central assumptions is not a commercial proposition. Even on the optimistic revenue and cost forecasts that Norman is putting forward the project falls below the 5 per cent real return test. The more probable outcome seems likely to be no more than zero, and it would not take much to cause the return to become negative.

I have in mind two main reasons for these doubts. First, it seems to me the calculations are based on optimistic views about likely cost developments. There are technical hurdles still to be overcome and experience, anyway on projects of this kind, normally shows unexpected cost escalations. But since the A 320 will be facing a dollar price fixed by Boeing, and I suspect at a time when the effective dollar exchange rate is weakening, it will not be feasible to pass these increases through into prices. Second, Boeing's selling competition is aggressive and has a record of success. I cannot see A 320 sales achieving anything like a sufficient level of sales (800 at least would be needed) to achieve an acceptable return.

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Norman nevertheless believes that we should accept the prospect of these disappointing returns to maintain a foothold in the international civil aviation industry and to preserve capacity for that purpose in this country. This raises some wider issues. To assist a project which is so commercially doubtful would be hard to reconcile with our general stance on Government assistance to industry. We have taken the view in the cases brought to our notice that there is no point in trying to preserve capacity and jobs in loss making industries. In the end this will only result in lost jobs elsewhere, and will undermine our economic performance. Moreover, to agree to support this project may make it much harder to resist the claims of other industries looking for Government support. So the cost to public expenditure of a wrong decision on the A 320 could turn out to be much more than the £220 million we are being asked to agree.

I am also unimpressed by the argument sometimes advanced for supporting loss making civil aerospace projects of technological spin-off to the rest of the economy. I am advised that wing development is not a high technology activity and that there would be little spin-off to the rest of the economy. I know that Robin Nicholson takes this view. Indeed it may be that the skilled labour which would be involved in developing the A 320 wing would be better employed in some other activity with a higher technological content and a better prospect of profitability.

Finally, I am sceptical of the argument that we must support the A 320 in order to maximise the V 2500's chances of being selected for the A 320. Engine selection for the aircraft will be made by the airlines and, although the French will try and push the claims of the CFM56, several airlines, such as British Airways, have said that there would be no point in purchasing a new technology aircraft unless it had a new engine in it. Furthermore, I question the extent to which the French could get away with discrimination against the V 2500 in commercial offers to airlines. The Germans, who will be partners<sup>in</sup> the A 320, and the Italians, who may be, are also participants in the V 2500 and will press the case for the V 2500. There is also the point that if Airbus hope to sell

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their aircraft in Japan and the USA they will not improve their prospects by blackballing an engine which will have more than a 50% Japan/USA content.

I am copying to E(A) colleagues.

A handwritten signature in blue ink, appearing to be 'PR' with a small flourish at the end.

PETER REES

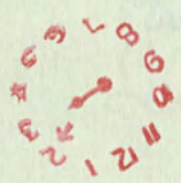
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