SECRET AND PERSONAL

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Prime Minister (2)

To note.

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

PRIME MINISTER

It seems to me that there [illegible] leave no room whatsoever for ingenuity in overcoming difficulties, but believe that there will need to be a meeting of the rail group before the end of next week; that there will be decisions to take.

THE RAILWAYS

At our meeting on 26 May I was asked to provide an analysis of the likely cost to other public sector industries of industrial action on the railways. I attach a note providing this information. The note has been prepared in consultation with sponsor Departments concerned but largely without consulting the industries themselves because of the sensitivity of the material. The figures are inevitably approximate and should be treated with caution.

MCS 10/6

2. The note makes some basic assumptions about the nature and duration of any industrial action. In particular, it assumes that the action will take the form of an all-out stoppage beginning in the first week of July (although an earlier start to the dispute or earlier limited action, such as overtime bans, are unlikely significantly to effect the estimates). It also assumes that sympathetic action by other unions will be limited allowing road haulage, for example, to be substituted for rail transport to the maximum extent feasible. On this basis, the attached note shows what might be the effect of a relatively short (one month) and long (3-month) dispute. Where an industry faces some critical point outside these parameters after which its costs escalate sharply, this is identified separately.

3. The note also distinguishes where possible between the immediate, gross, costs of any dispute and the net effect on EFLs which will reflect the extent to which losses have been recouped (or exacerbated, for example by lost markets) during

the remainder of the financial year. For the purposes of this exercise because any cost would influence the demands they make on the Government it treats British Leyland, British Nuclear Fuels Ltd. and Rolls-Royce as public sector bodies although the financial effect is significant only in the case of British Leyland.

4. The clear message of the note is that the potential costs to Government finances of a long rail dispute is extremely high - possibly in excess of £1 billion if the dispute lasts 3 months. Two factors account for the great bulk of this cost. First, we have assumed that maximum oilburn is to be started at the outset of the dispute. This alone accounts for about one-third of the total cost to the public sector, although in terms strictly of lasting out a rail strike, it may not be necessary to begin oilburn so early or at such a high level. A lower level of oilburn, or a later start, would have implications for the level of coalstocks which could be rebuilt by the Autumn but would significantly reduce the costs of a dispute. I think it would be helpful if Nigel Lawson could provide an assessment of the effect of significantly lower levels of oilburn, or of starting maximum oilburn later, on our ability to endure a rail strike and subsequently on the level of coal stocks. We can then consider where our priorities lie.

5. The second major contributor is British Steel. The very substantial costs BSC expect to incur (£500 million for a 3-month strike) apparently stem from their decision to handle a rail strike by progressively shutting down their business altogether. This tactic may make commercial sense in the context of a relatively short dispute when relatively high stocks and the approaching holiday season will ensure that costs are minimised. Even over a 2-month period the costs of this approach, while severe at £100 million or more, would be containable. With a 3-month strike, however, there is a danger that BSC's tactics would backfire. As stocks ran down and markets were progressively lost, revenue losses would mount

and, having shut down, there would be difficulties in restarting production during a rail strike. The resulting prolonged shutdown would have a devastating effect on BSC's finances. In view of the possibility of the stoppage being a long one, I think it would be helpful if Patrick Jenkin could ascertain urgently whether an alternative strategy, based on maintaining production, exists for BSC and whether such a strategy would mitigate the financial consequences set out here. We would then be in a position to consider whether there should be discussions with BSC about the course they should adopt in the event of a rail strike.

6. I am copying this minute to Willie Whitelaw, Patrick Jenkin, Nigel Lawson, George Younger, David Howell, Arthur Cockfield and to Sir Robert Armstrong and Mr Sparrow. Its circulation within Departments should for obvious reasons be extremely limited.

GH

(G.H.)
10 June 1982

EFFECT ON OTHER PUBLIC SECTOR INDUSTRIES ON INDUSTRIAL ACTION ON THE RAILWAYS

The industries most affected by a stoppage on the railways would be:

National Coal Board
Electricity Supply Industry
British Steel Corporation
British Shipbuilders
Post Office
British Leyland

A number of other industries, such as National Bus and British Telecommunications might indirectly benefit, for example from increased traffic, but the financial effects are likely to be marginal.

This cost to British Rail (BR) itself of any dispute would depend crucially on which of its unions participated. If both NUR and ASLEF members strike (but not the administrative staff (TSSA) or engineers (AUEW)) the net cost to BR would be about the same as the loss now incurred in operating the railway - ie the effect would be zero in EFL terms, although the Board would be faced with the problem of how to finance losses of £15-16 million a week if the Government ceased paying grant. If ASLEF alone take strike action, the EFL cost would increase to £12m a week, an underlying loss to the Board of £27-28 million. The Secretary of State for Transport will be bringing forward a separate note dealing in more detail with the effect of a dispute on BR's finances.

The effect on other public sector industries is summarised in the table below. The position of each industry is described in more detail in the notes which follow.

	1 month strike		3 month strike	(£ million)
	Immediate gross cost	Likely net EFL effect	Immediate gross cost	Likely net EFL effect
National Coal Board) Electricity Supply)	N/A	150	N/A	470
British Steel	80-120	40-60	350-450	500
British Shipbuilders	Negligible		15	15
British Leyland	0-40	n/a	Up to 100	n/a
Post Office	Negligible		25	Less than 25

National Coal Board and Electricity Supply Industry

The close links between these two industries make it necessary to consider them together.

The crucial assumption is that the CEGB maximise oilburn from the outset of industrial action. This will cost £30 million a week - £120 million for a one-month dispute and £360 million for a 3-month dispute. If the CEGB hold to their agreement to take 76 million tonnes of coal from NCB in 1982-83 despite the increased oilburn, all these costs will fall on the CEGB. To the extent that the CEGB takes less coal in total during 1982-83 (and it is doubtful whether it would be physically possible to deliver the planned full amount after a 3-month stoppage) part of the cost will fall on NCB. But the overall cost to the public sector will ramain unchanged.

In addition, certain costs will inevitably be incurred by NCB. Coal not delivered to the CEGB during the dispute, even if it is delivered later, will have to be stocked. Additional stocking will also result from lost sales to other customers where alternative transport cannot be found (put at 250,000 tonnes a week or 50 per cent of sales). In the case of non-CEGB customers there will also be an irrecoverable revenue loss to the extent that sales are note recouped at a later date. These costs are likely to total £30 million for a one-month strike and £90 million for a 3-month strike.

The Scottish Electricity Boards would not suffer any adverse financial impact from a dispute. It is assumed that non-rail coal deliveries are maintained and maximum use is made of the interconnector to supply

CEGB. In these circumstances only a 3-month strike would require increased oilburn in order to maintain coal stocks above 1.5m tonnes. However the cost of this oil burn (£20 million) would be passed on to the CEGB and is taken into account in the cost estimates given for that industry.

British Steel

In the event of a rail strike BSC intend to close down all their major steelworks progressively, in an orderly fashion. BSC's main steelworks depend on rail deliveries of their bulk raw materials - iron ore, coking coal and fuel oil - and transport of semi-finished steel between BSC works and to private sector steel processors is also predominantly by rail. The advantage to BSC of an orderly closedown is that, once the rail strike is over, they would be able to resume full normal production quickly and efficiently.

A rail strike from 1 July which only lasted one month would occur at a period when BSC order books are low, and planned holiday shutdowns are due to occur. A large proportion, probably half, of the gross costs of a strike could therefore be expected to be recouped. It would be difficult for BSC to recoup even these net losses of £40-60m by means of any subsequent action.

The critical point for BSC would come after about 2 months. Up till the end of August, with planned holiday shutdown periods and low orders and deliveries expected, the effects would be fairly expensive (perhaps £100 million to £200 million net) but containable. But if production were not restored early in September BSC would begin to experience very serious effects. A three-month rail strike would be extremely serious. The gross cost would be about £35 million a week after the first month; at a rough estimate the gross cost over 3 months would be £350 million to £450 million. But since imports of finished steel are usually carried by road there would be further costs since BSC would lose UK market share and export business from such a prolonged shutdown: a 10 per cent drop in BSC's steel deliveries (equivalent to roughly 5 per cent loss of UK market share) would cost BSC about £100 million a year. If this business could not be won back reasonably quickly the viability of some of BSC's major plants would be put at risk, with the possibility of major closures. A three-month strike which kept BSC shut down would probably cost BSC about £500 million in 1982/83 with no possibility of recouping any of these losses either in 1982/83 or in subsequent years: indeed there would probably be on-going costs from permanent loss of steel business.

British Shipbuilders

It is believed that British Shipbuilders (BS) would be relatively unscathed by a one month strike. Those yards where steel is delivered by train and other forms of transport could not easily be substituted should be able to minimise costs by re-ordering work programmes (eg to enable outfitters to start work early on unfinished vessels). This process could not however be maintained indefinitely. A 3-month strike would be likely to cost £15 million mainly in overheads and wage costs in the yards affected. These costs would be a once and for all effect - the net cost would also be in the region of £15 million. BS do not believe these costs could be recouped readily.

The crucial assumptions in this are that road haulage is unaffected; and that supplies of steel continue to be available. The assumption of continued road haulage has been made in all cases and is judged a reasonable one. The assumption about steel supplies is more problematic. British Steel do not envisage continuing large-scale production in the event of a strike. British Steel's stocks are relatively high; and BS carry a further one month's stock themselves. But should it prove impossible to procure alternative steel supplies (eg, from abroad) when these stocks are exhausted the effect on BS could be severe. The financial cost would not be less than £50 million a month.

British Leyland

The cost estimates of £0-40m and up to £100 million for a one and 3-month strike represent what is known to be at risk in terms of vehicles exported which are currently transported by rail. To the extent that alternative forms of transport can be found, the cost will be nearer zero than £40 million for each month.

In addition, BL are likely to face costs in maintaining production in the face of supply difficulties - rail transport plays an important role in the assembly process. No estimate of these costs is available, but after 3 months BL could well be facing difficulties in maintaining production with consequent risk of market losses and increased financial costs. The estimates given here should therefore be regarded as a minimum.

The costs to BL of a rail dispute will not necessarily be equivalent to the costs to Government. An estimate of these latter costs could not be made without detailed discussions with the industry about its likely response to industrial action.

Post Office

It is believed that the Post Office could contain the effects of a one-month stoppage by using alternative means of transport. Over a 3-month period, this would have an increasing cost, although the net cost to the Post Office will be much lower to the extent that they can negotiate compensation from BR. A 3-month strike, however, would increasingly affect service quality leading to some traffic loss and consequent revenue loss.

It is a crucial assumption for the Post Office that all other means of transport remain available to carry additional traffic. If this were not the case, the cost of a 3-month strike would reach £100 million.

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SCJV

Prime Minister (2)

MES 15/6

CABINET OFFICE

Central Policy Review Staff

70 Whitehall, London SW1A 2AS Telephone 01-233 - 7798

Qc.03064

15 June 1982

Dear Chancellor,

The Railways

John Sparrow saw your minute to the Prime Minister of 10 June before he went on leave, and asked me to let you have some CPRS comments. We have also seen the letter of 14 June with the Prime Minister's comments.

2. Extra oil burn accounts for one-third of the cost to the public sector, on the assumption that it begins from the start of a rail dispute. But as your paper notes, a later start or lower level of oil burn would be possible. A decision by Ministers to authorise extra oil burn should follow from an up-to-date assessment of all the relevant factors, including the likely length of a rail strike, the risks of a miners' strike in the autumn, and the relative importance of varying coal stocks on both fronts. The CPRS agrees that it would be helpful if the Secretary of State for Energy could produce the up-to-date assessment of coal stocks and the effects of oil burn suggested in your minute.

3. Secondly, the CPRS agrees that the BSC figures are disturbing, and would question BSC's approach to what may well be a long dispute. Two of BSC's integrated plants, Port Talbot and Teesside, are on coastal sites and may not be so dependent on rail supplies of raw materials. We also understand that part of BSC's dependence on rail is for movement of semi-finished steel from site to site: much of this semi-finished steel might be transferred by road, even if it means operating the finishing plant at less than optimum levels. It is quite possible that by these means BSC could sustain a sizable proportion of its business during a rail dispute. We agree that the Secretary of State for Industry should ask BSC to examine an alternative strategy, based on maintaining production so far as possible, and assess its financial consequences.

4. I am sending copies of this letter to those who had copies of your minute.

Yours sincerely,

Alan Bailey

A M BAILEY

SECRET AND PERSONAL

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hc: J. Vereker.

10 DOWNING STREET

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Energy
SO
Transport
Trade,
CO
CPRS

From the Private Secretary 14 June 1982

Dear John,

THE RAILWAYS

The Prime Minister read with interest the Chancellor's minute of 10 June about the likely cost to other public sector industries of industrial action on the railways.

She has commented that the figures in the Chancellor's note appear to take no account of savings which will accrue from ingenuity in overcoming the difficulties. The Prime Minister therefore agrees with the Chancellor that it will be helpful if the Secretary of State for Industry could ascertain urgently whether an alternative lower cost strategy exists for BSC; and whether similar moves could be made elsewhere to minimise the cost of industrial action. It would clearly be useful if this were available for the meeting arranged for Thursday 17 June.*

B/F

I am sending a copy of this letter to the Private Secretaries to the Home Secretary, the Secretaries of State for Industry, Energy, Scotland, Transport and Trade, Sir Robert Armstrong and John Sparrow (CPRS).

Yours sincerely,

Michael Scholar

* but now postponed until early next week.

John Kerr, Esq.,
HM Treasury

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