



Secretary of State for Industry

INDEX.

A General brief re <u>discussions</u> with

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PS/SECRETARY OF STATE

cc PS/Minister of State (Mr Lamont) PS/Mr Butcher PS/Secretary Mr Manzie Mr Farry

We spoke late last night about the request from No 10 for a Speaking Note for the Prime Minister's meeting with the TUC Delegation. This is attached together with a Confidential Note which advises the Prime Minister not to reveal the current assistance being contemplated from Defence Votes.

A C RUSSELL US/SBP

US/SBP RM 160 ASH 212 6296

27 July 1982

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CONFIDENTIAL

The Secretary of State for Industry and the Secretary of State for Employment saw Lord Matthews yesterday and put to him that £4m might be available from Defence funds if the vessel was ordered in the UK and there could be guarantees about its availability both in a national emergency and for exercises two or three weeks each year.

The Cunard response was perhaps predictably that this money was nowhere near sufficient, and they asked for the possibility of soft loans by BS to be taken into account and for their compensation claims consequential upon the loss of the Atlantic Conveyor to be treated sympathetically.

Officials from DOT, DOI and MOD are meeting Cunard on Tuesday 27 July 1982 to discuss and evaluate Cunard's response. After a report-back to Ministers it is likely that there will then have to be another meeting between Lord Matthews and the Secretary of State for Industry.

The Prime Minister is strongly recommended not to reveal to the delegation the offer so far to Cunard of £4m. Now talk of £3m being offered by MOD has appeared in the Press, it would be very difficult next day to reveal that £4m has been offered. Ascending offers of money only weakens the negotiating stance of the Government which can only be maintained if the Government gives an impression that the Government is prepared to see the order go if the Cunard price cannot be reached without excessively high levels of subsidy. Moreover sunless Cunard softens its present position, the Government will be faced with a difficult choice.



PRIME MINISTER'S MEETING WITH TUC DELEGATION CUNARD/ACL ORDER

SPEAKING NOTES

I fully recognise the importance of this order to the shipbuilding industry and the industries supplying the shipbuilding industry.

RELATION TO FALKLANDS

We also very much appreciate the strength of feeling that the order has aroused because it has been linked with the loss of the Atlantic Conveyor in the Falklands. In fact however before the Falklands crisis, Cunard together with their fellow shareholders were considering a modernisation plan to replace six ships of which the Atlantic Conveyor was one, with five more efficient ships, and before the Falklands conflict, arrangements were being made to sell the Atlantic Conveyor. Nevertheless we fully recognise from a defence point of view the excellent service rendered by the Atlantic Conveyor and the importance to Defence of having available in any future emergency, vessels like the new Cunard ship.

PRICE GAP

The main difficulty in this case as Lord Matthews has said on a number of occasions is the large price gap between BS and its competitors. I am not going to comment at this stage on the size of the gap though there have been various figures suggested in the Press, but the BS price has not been the best in Europe. However as Lord Matthews has also made clear the real competition is not with Europe but with the Far East. The price gap arises after BS has taken into account Intervention Fund assistance whose purpose is to help them to meet Far Eastern competition, and the availability of the Home Credit Scheme which makes available to British shipowners



ordering in British yards the terms which they can get if they order overseas.

GOVERNMENT TRYING TO FIND A WAY TO BRIDGE THE GAP

The Government is exploring ways of bridging the gap, and is anxious to find a solution. There are currently talks with Cunard between DOI, the sponsor Department for shipbuilding, the Department of Trade, the sponsor Department for shipping, and the Ministry of Defence. The excellence of the Atlantic Conveyor's service in the Falklands and the interest which the Ministry of Defence have in the availability of large modern merchant ships in times of national emergency, make it entirely appropriate that in this case Defence considerations should be taken fully into account. Cunard are not expected to reach a decision on the order until towards the end of this week so that there is time for the Government's initiative to be fully considered by Cunard.

WILL THE GOVERNMENT'S INITIATIVE BE SUCCESSFUL?

I cannot however forecast whether the current discussions will result in good news. There must be a limit to what the Government can pay to obtain a single order or to the amount of subsidy which can be paid to a single industry. We have paid approaching £600 million to the shipbuilding industry since coming into Office and this is proof of the Government's intention to help the industry towards viability. But as I have indicated it is the Government's hope that a way will be found to bridge the gap though I cannot guarantee the outcome of present talks. The unwelcome position is that the price gap between British Shipbuilders and its Far Eastern competitors is large.

DEFENSIVE

WILL THE PRIME MINISTER CONFIRM WHETHER £3M HAS BEEN OFFERED TO CUNARD?

I do not think that it would be right to comment on figures which appear in the Press, while discussions are going on with Cunard. When discussions have been completed I will of course give as



full an account as possible consistent with the needs of commercial confidentiality.

WHAT ABOUT THE EEC LIMITATIONS?

EEC limits on subsidies for shipbuilding is certainly a difficulty which restricts our room for manoeuvre in bridging the gap. The Government supports the Community policy of reducing subsidies for shipbuilding. It is in the shipbuilding industries' own interests and excessive subsidisation is also harmful to shipping. We must certainly not give shipbuilding jobs a higher priority than shipping which is a very large and important industry to this country in its own right. But because of the Falklands link to this case which so clearly demonstrated the potential usefulness of ships such as this order, there are Defence considerations which also have to be taken into account in this case.

DOES THIS SIGNAL A NEW DEPARTURE IN GOVERNMENT POLICY IN ATTACHING DEFENCE CONSIDERATIONS TO ORDERS BY UK SHIPOWNERS?

There are special considerations in this case resulting from the service given by Cunard ships in the South Atlantic and this is amply demonstrated by the strength of feeling which has led to the TUC bringing a delegation to me. I do not therefore think that this case should be regarded as a precedent.

CAN COMPENSATION BE USED TO INFLUENCE THE CUNARD DECISION?

Cunard have a legal right to the compensation which has been paid on the Atlantic Conveyor and in any event it would be totally wrong to attempt to put an illegal fetter on the compensation due to them to put pressure on Cunard to "buy British".

WHAT ABOUT HEAVY SUBSIDIES ABROAD?

We certainly keep a very close watch on the practices of other European countries but as I have indicated the real competition in this case is not with Europe but with the Far East. The subsidies given to our shipbuilding industry compare very





favourably with those given by other countries to their industries. While for example Sweden gives generous aid to domestic shipowners, their shipbuilding industry does not have direct production subsidies.

CONFIDENTIAL cc PS/Secretary of State PS/MINISTER OF STATE PS/Mr Butcher PS/Secretary (Mr Lamont) Mr Manzie Mr Atkinson NERO Mr Beale MEETING BETWEEN THE PRIME MINISTER, MINISTER OF STATE AND DR DAVID CLARKE MP 29 JULY 1982 REDUNDANCIES AT TYNE SHIPREPAIR GROUP brief.

I think a somewhat fuller brief is needed than that submitted by Mr Beale in his minute of 26 July and I attach a revised

A C RUSSELL

US/SBP RM 160 ASH 212 6296

27 July 1982



PRIME MINISTER AND MR LAMONT'S MEETING WITH DR DAVID CLARKE MP 29 JULY 1982

BACKGROUND

BS announced on 15 July contraction of their shiprepair activities affecting mainly Tyne Shiprepair Limited which currently employs 2500. The company is to be concentrated at Wallsend Dry Docks on the North Bank of the Tyne and three shiprepair establishments in Dr Clarke's constituency are to close. The total reduction of the labourforce could be up to 1,400 men. Discussions with the unions are to take place soon at yard level. (A copy of the BS Press Notice announcing the contraction is attached).

Dr Clarke can be expected to argue that because of the very high unemployment in the constituency the closures should be postponed and that in any case they are due to the reduction in BS's loss limit from £25m last year to £10m this year.

POINTS TO MAKE

- (i) Tyne Shiprepair has been lossmaking every year since Vesting Day and losses increased from £5.3m in 1980/81 to £7.9m last year. BS regard these losses as unacceptably high.
- (ii) There have been numerous causes of complaint by private sector shiprepairers that BS has been taking business at a loss and competing unfairly. Practically all these complaints on investigation were about contracts taken by the Tyne Shiprepair Group. It is difficult to judge whether a particular price is unfair because shiprepair consists of one off jobs. But the strongest evidence is the very high rate of loss at Tyne Shiprepair which no private



company could sustain for a year.

- (iii) Keeping open the over capacity in BS shiprepair would therefore be only too likely to damage private sector shiprepair companies and this point was recognised by the Industry and Trade Select Committee's first Report on British Shipbuilders early this year who stated that "they would wish to see the clearest evidence within the next year that BS have started to carry out their Chairman's intention of closing, selling or getting rid of any company which continues to show no sign of viability. Meanwhile tendering at below cost should cease."
- (iv) This Government has endeavoured to help the shiprepair industry. In 1979 this Government extended the Home Credit Scheme for UK owners to cover conversions on ships costing over £lm. On Monday the Minister of State announced that credit on conversions for UK owners would be increased from 5 years to 8½ years.
- (v) Substantial aid is going to Tyneside, apart from the very substantial support to shipbuilding, the Government has provided £58m to Tyneside in Regional Development Grants and offers of Selective Financial Assistance indeed the latter is estimated to have safeguarded around 9000 jobs and directly created about 3000 jobs.
- (vi) As part of our policy of concentrating assistance on areas of greatest need the Government is on 1 August reducing the coverage of assisted areas from nearly a half of the population to just over a quarter and this will naturally enhance the attractions of Special



Development Areas such as Tyneside and South Shields.

DEFENSIVE

HOW CAN BS CONTRACT THEIR SHIPREPAIR ACTIVITIES WHEN THEY HAVE A STATUTORY DUTY TO HAVE FULL REGARD TO THE REQUIREMENTS OF NATIONAL DEFENCE IN ALL THEIR ACTIVITIES?

BS of course consulted the Government whether there are Defence implications in their restructuring plans for shiprepair but there is ample capacity in shiprepair taking account of capacity in the Royal Dockyards and indeed Chatham Dockyard has to go because there is surplus Royal Dockyard capacity.

ARE BS WILLING TO SELL THE YARDS TO PRIVATE SHIPREPAIR COMPANIES?

The Government position is that if the private sector is willing to take on any of these facilities, they would be most welcome. It is the employment which would be offered that is important and the Government would certainly be prepared to talk to British Shipbuilders if they need any persuasion to be willing to sell. However the position is that so far it is too early to tell whether the private sector is going to be seriously interested.

itish Shipbuilders

THURSDAY, JULY 15, 1982

BS SHIPREPAIR RESTRUCTURING

British Shipbuilders announced today that, as a result of appalling market conditions and consequential adverse financial performance in the Shiprepair sector, they are restructuring shiprepair companies on the Tyne, Tees and at Grangemouth.

British Shipbuilders has made strenuous efforts to achieve financial viability overall and its performance has improved dramatically with losses being reduced from £108 million in the first year of operation to a limit for the current year of £10 million.

Considerable success has been achieved throughout the Corporation, but shiprepair remains a difficult area. This is caused by the worldwide recession which has affected shipping, which in turn means that there is only limited, and highly competitive shiprepairing business available. This is a problem common to the industry worldwide, but particularly in Western Europe.

However, in certain areas of the UK there are additional problems such as the geographical location of some repair facilities in rivers or estuaries where the traditional shipping trade has been reduced, thus limiting the possibilities of voyage repairs, etc..

For further information:

Benton House, 136, Sandylord Road, Newcastle upon Tyne, NE2 1QE Tel: Newcastle upon Tyne (0632) 326772 197, Knightsbridge, London SW7 1RB Tel: 01-581 1393

Because of all these factors, the Shiprepair Division has been sustaining heavy losses, of more than £1 million per month in recent times. Clearly figures of this order threaten the objective of achieving viability, and would undermine other parts of the industry.

The action now being taken is intended to correct the situation taking into account the adjustments needed to cover the long-term effects of the changes in the market and to match the repair facilities offered by British Shipbuilders to the requirements of the shipping industry.

In this way, shiprepair will continue to provide services and facilities competitive with other parts of Western Europe and offer a long-term future for the companies and security for their employees.

Regrettably, the changes now being introduced could involve a total of more than 1,500 employees at the yards affected.

Every effort will be made to minimise the effect on individuals and, in the first instance, the Corporation will so far as possible offer transfer and voluntary redundancy where appropriate.

Following meetings with the Shipbuilding Negotiating Committee of the Confederation of Shipbuilding and Engineering Unions, and discussions which will now take place at yard level, the situation will be kept under close review during the next three months.

It hould be stated that British Shipbuilders firmly intends to remain in the shiprepair business, in accordance with its statutory duties under the Aircraft and Shipbuilding Industries Act 1977.

The detailed changes are :

Vosper Shiprepairs Ltd., Southampton: No change in labour force

but continued urgent

efforts to reduce overheads.

Falmouth Shiprepair Ltd. Falmouth : No change.

Grangemouth Dockyard Ltd. Grangemouth: Labour force to be reduced by 40 to 95.

Smith's Dock Ltd. Middlesbrough

in shipbuilding and this will remain unchanged, but it will cease shiprepairing, and about 100 employees could be affected.

Tyne Shiprepair Ltd.

: Shiprepair to be concentrated on North Bank of River Tyne in Wallsend Dry Docks. Labour force could be reduced by 1,400 together with other urgent efforts to reduce overheads.



NOTES ON SUPPLEMENTARIES

SHIPREPAIR

- Q: WILL THE PRIME MINISTER INSTRUCT BS NOT TO RESTRUCTURE ITS SHIPREPAIR ACTIVITIES TAKING INTO ACCOUNT BS'S STATUTORY DUTY TO HAVE REGARD TO THE REQUIREMENTS OF NATIONAL DEFENCE IN ALL ITS ACTIVITIES?
- A: No Sir. In the Government's view there are no Defence considerations which would warrant such action taking into account the capacity at the Royal Dockyards.

The Government supports the recommendation of the Industry and Trade Committee that BS should close or dispose of shiprepair interests which show no sign of becoming viable.

- Q: WILL THE GOVERNMENT TAKE STEPS TO STOP UNFAIR COMPETITION FROM BS?
- A: The Chairman of BS regards the heavy losses in ship repair as unacceptable, and the steps announced last week are evidence of his determination to bring BS's shiprepair activities into viability.

We do not wish to see the private sector ship repair undermined by a lossmaking public sector, and his determination to restore profitability is welcome. The heavy losses in shiprepair have been of great concern to the Government and the private sector. Around £50m has been lost on ship repair by BS since Vesting Day.

- Q: DO NOT THE SHIP REPAIR REDUNDANCIES MAKE IT ALL THE MORE IMPORTANT FOR BS TO OBTAIN THE CUNARD/ACL ORDER?
- A: It goes without saying that the Government would very much prefer this ship to be built in a British yard and as the Minister of State, Mr Lamont, told the House last night there are continuing talks with Cunard on how the present large gap might be closed and the Government is anxious that a way will be found.



Q: <u>INADEQUATE HELP FOR BS?</u>

A: BS have the advantage of the Intervention Fund, Shipbullders Relief, and being financed by Public Dividend Capital which is unremunerated. Approaching £600m has been provided to BS through Public Dividend Capital, Intervention Fund and the Shipbuilding Redundancy Payments Scheme. There must be limits on the amount of subsidy going to a single industry, and our policy is to reduce subsidies and BS8s dependence on the Exchequer. Considerable progress has been made, but the amount of shipbuilding aid still compares favourably with that given by foreign Governments to their shipyards.

- Q: IS BS's LOSS LIMIT THIS YEAR OF £10M IN DANGER OF BEING EXCEEDED?
- A: BS have told us that they think they can meet it.



DRAFT

Addressed to:

The Chancellor of the Exchequer

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SECRETARY OF STATE (Initials and date)

DEPARTMENT OF INDUSTRY

CUNARD/ACL ORDER

Officials from the Department of Industry, the Ministry of Defence and the Department of Trade had discussions today with Cunard to explore further the Cunard response to the offer of £4m from Defence Votes which Norman Tebbit and I put to Lord Matthews yesterday on condition that the ship would be available in times of emergency and also for annual exercises for a period of say two to three weeks per annum.

Lord Matthews' initial response to our offer was predictably that it was too small to come near bridging the gap, and it would be necessary for the Government to top up its offer either through the compensation route, or from extra money coming from the Defence Votes, or from soft credit to be made available through BS.

The discussions at official level on the availability of the ship for Defence purposes made some progress, and provisional Heads of Agreement are attached.



However, despite being pressed very hard by MOD officials, Cunard were not prepared either to guarantee the availability of the ship at short notice in conditions short of national emergency or to any limitation of their total freedom to sell or otherwise dispose of the ship with no refund of money to MOD.

As regards the issue of compensation Cunard have put in a claim to the Department of Trade for consequential losses arising from the loss of the Atlantic Conveyor. The largest item is for \$4m to cover the increased cost to them of purchasing a ship from one of the other members in the ACL Consortium. Cunard say that they have a strong moral claim for such a payment, but they recognise that their legal position may not be. If therefore the Government were to meet this claim, they would regard the payment as being a Government contribution towards bridging the gap without prejudice to pursuing their claim if the Government does not feel able to offer the \$4m as part of the total package. Whether there are any other additional ways of closing the gap between the BS bid and the Far East through the compensation route is for consideration.

The attached schedule shows how the gap could be reduced if Ministers could use the compensation route and other inducements to Cunard. Rescheduling of instalments payments under normal Home Credit rules present no difficulty, but it is also for consideration whether to offer Cunard additional rescheduling which would allow Cunard to pay nothing before delivery.

If all the items in the list were authorised, and Lord Matthews agreed to buy at a PDV value of \$50M as he has hinted, it would only be necessary

8

to reduce the gap to \$2.3M.

However Cunard at present are saying at senior management level, that they would need the MOD contribution of £4M, compensation inducements of \$4m, plus an interest free loan from BS of around £4m. They are concerned whether the MOD contribution would be liable to tax.



CLOSING THE GAP IN PDV TERMS			
BS Korea 47.7	Gap 24.2	≸M	
Less MOD contribution of \$7.04m (£4m) which is worth \$9.2m in NPV	15		
(b) Less Compensation \$4M which is worth \$5.2m in NPV	9.8		
(c) Less Rescheduling of payments under normal Home Credit Rules worth \$3.2m	6.6		
(d) Less Further rescheduling with Cunard paying nothing before delivery \$2.4M	4.2		
(e)Less Paying Cunard Marine Risk Insured Value on Atlantic Conveyor \$2.lm worth \$2.8M	. 1.4		
122 postular imposement.	4	47.7 24 22 muss	6
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PROVISIONAL HEADS OF AGREEMENT BETWEEN THE MINISTRY OF DEFENCE AND CUNARD LIMITED REPLACEMENT FOR THE ATLANTIC CONVEYOR Cunard undertake: 1) To agree, subject to detailed investigation, to incorporate in the initial design of the G3 replacement ship for the Atlantic Conveyor modifications to improve its adaptability for military use, on the understanding that identifiable additional costs will be met by the Ministry of Defence and that the modifications will not involve detriment to the commercial operations of the ship or delay its planned entry into service; 2) To make this ship available to the Ministry of Defence for up to five weeks per annum from its entry into service (planned for August 1984) so long as it remains in Cunard ownership, subject to a minimum of twelve months notice by the Ministry of Defence and the payment of normal market charter rates: To make available in the Spring of 1983 on the same 3) basis as (2) above, the Atlantic Causeway (G2 ship); 4) That if for any reason the G.3 replacement ship is not available, to use their best endeavours to make a GI or other suitable ship available on the same basis as in (2) above; Not to dispose of the ship without prior consultation with the Ministry of Defence.

\$16.6

MR HARDBATTLE, PARLIAMENTARY BRANCH

cc PS/Secretary of State
PS/Minister of State
(Mr Lamont)
PS/PUSS - Mr Butcher
Mr Manzie, Dep Sec
Mr Russell, SBP
Mr Broomfield, SBP3

PM'S QUESTIONS - 22 JULY 1982 CUNARD/ACL ORDER

No 10 will have had our briefing for the PM's meeting with the TUC. This material can be drawn upon for questions this afternoon.

You told me that No.10 nevertheless wished to have additional briefing on a number of points. For this purpose I attach the following:-

Table 1 - Prices and deliveries.

It should be noted that the position can change very rapidly in the light of the efforts being made to secure the order for BS.

Table 2 - Subsidies available for the order.

Table 3 - Redundancies in BS
Breakdown of BS's costs
BS's competitiveness.

Milay.

M E FARRY SBP1 Rm 162 Ashdown 212 5997

27 July 1982

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COMPARATIVE BIDS CUNARD/ACL PRICES

	Cash &	PDV of Cash (PDV Present Day Value)	ZM Credit Charges	Supervision 5	Positioning #	Total PDV	Deliveries
BS	79 (£45.7m)	65.9	5.5	0.5		71.9	26 ^(a) months
Korea	50	44.6	0.9	1.1	1.1	47.7	22 months
Japan	54	47.6	1.0	0.8	1.0	50.4	18 months
France(b)	69.85	65.0	3.1	0.5		68.6	27 months



⁽a) BS delivery improved to August 1984 26 months on assumption that they will gain technical cooperation from Swedes.

⁽b) The French prices are now out of date and the French are negotiating direct with CGM the French shipping line.



SUBSIDIES AVAILABLE UNDER SHIPBUILDING SUPPORT SCHEMES

		(of contract price)
Intervention Fund	£6.9m	15%
Shipbuilders Relief	£0.9m	2%
	£7.8m	17.0%
Home Shipbuilding	æ/•OIII	11.0%
Credit Scheme	£6.2m	13.5%
	£14.0m	30.5%

Note: Public Dividend Capital does not enter directly into the subsidisation of individual orders. PDC is used to meet cash needs for investment and to cover losses incurred by BS as a whole from unrecovered overheads due to capacity underutilisation as well as losses on individual contracts.

Sums approaching £600m have been provided to BS by the present administration. The breakdown of payments made from 1979/80 to date is:-

	£m
Intervention Fund	125
Public Dividend Capital (PDC)	418
Shipbuilding Redundancy Payments Scheme	51
	£594m



TABLE 3

Redundancies in BS

1980	1981	1982		
8,300	3,300	560	announced in on Tyneside)	

Breakdown of Costs

British Shipbuilders have said that their bid is made up of:-

			£m
	Materials	3	27
	Labour		14
	Overheads	3	12
		Total	53
less	Intervention	Fund	7
		Bid	£46m

The Japanese and Korean prices Cunard have quoted are around £30m. This is little more than the price BS say they have to pay for materials - about 90% of which are bought in the UK. Considerable reductions in overhead and labour costs would therefore be needed to make the bid comparable. BS's building time is however many months longer than the Far Eastern yards and this must have a sizeable effect on the gap.

There has been no suggestion of a wage cut to help win the order.

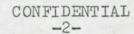
It is unlikely that the cost of restrictive practices (which BS are tackling) could have had a substantial effect on the price offered.

Improvement in competitiveness

Merchant productivity at BS fell during the worst of the recession but has improved over the last 2 years as the intake of orders has improved and the yards have been better loaded. But the overall level has still to surpass pre-nationalisation levels.

Throughput/employee year in merchant yards (compensated gross registered tons)

1978	15.3
1979	13.2
1980	15.0
1981	16.7





New orders in 1981 were nearly 20% up on 1980 and two thirds were for export reflecting BS's success in revitalising their export marketing efforts. In what is now a weak world market orders so far this year have been poor.



CUNARD ACL ORDER

- Q COMPONENTS OF GOVERNMENT ASSISTANCE TO BRITISH SHIPBUILDERS
- A Sums approaching £600m have been provided by the present administration. The breakdown of payments made from 1979/80 to date is:-

	£m
Intervention Fund	125
Public Dividend Capital (PDC)	418
Shipbuilding Redundancy Payments Scheme	51
	£594m



Background Note

The whole of the £418m in PDC indicated above has been paid out to BS.

A number of nationalised industries are given access to PDC by statute. PDC is equivalent to an equity holding entitling the Government to draw a dividend. While PDC bears no interest it is envisaged that the average level of dividend payments taking good and bad years together should be at least as much as interest on loans from the National Loans Fund. However in October 1979 Mr Butler told the House that until BS was profitable it would not pay dividends.