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PRIME MINISTER

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cc PS/CST
PS/EST
PS/MST
Mr Middleton
Mr Bailey
Mr Byatt
Sir T Burns

Mr Anson
Mr Cassell
Mr Christie
Mr R H Wilson
Mr Morgan - o.r.
Mr Turnbull
Mr Grimstone
Mr Burgner

COMPETITION AND PRIVATISATION

Privatisation, combined with increased competition, is one of the main planks of our economic policy. It is designed to improve our national economic performance by increasing the role of market forces and by reducing the size of the public sector. We made a good start during the last period of Government. But experience shows that much preparation and discussion are needed to prepare State industries and trading bodies for sale to the private sector. And after 3-4 years, an approaching General Election casts a forward shadow that makes further sales difficult. So we need to use the time we have available as fully and constructively as possible.

2. The programme we have put forward is a full one. The Manifesto speaks of selling 51 per cent of shares in British Telecom, Rolls-Royce, British Airways and substantial parts of British Steel, British Shipbuilding and British Leyland; privatising as many as possible of Britain's airports; introducing substantial private capital into National Bus; the transfer to the private sector of the British Gas Corporation's offshore oil interests; and increasing competition and attracting private capital into the gas and electricity industries. The Queen's Speech added the Royal Ordnance Factories. And there are other candidates also, as the papers circulated to E(DL) shortly before the Election showed.

3. Two aspects of the programme will become much more prominent in the next phase of our drive for privatisation.

4. First, the need to promote competition to the maximum extent means that we must give much more attention to the structure of the bodies which are on the privatisation programme. Hitherto the companies we have sold have mainly been profitable and operating in competitive environments. Preparing them for privatisation, although time-consuming in terms of legislation and preparations for flotation, has involved relatively little change to their structure. But from



now on we are increasingly working in the heartland of the public trading sector, where we shall have to deal both with the giant utilities and unprofitable companies. Questions of whether and how to separate the profitable parts from the unprofitable; how to separate the potentially competitive parts from the natural monopolies; and how to deal with the irreducible elements of monopoly will increasingly dominate the debate. We shall increasingly have to devote time and effort to these issues - well in advance of the mechanics of privatisation itself - if we are to reap the maximum benefit from a transfer to the private sector.

5. I recognise that in some cases the costs - in terms of the delay and upheaval involved in restructuring - of pursuing the best solution may be excessive, running the risk of putting off privatisation into the remote future. This is a price which in political terms we may not be prepared to pay. In particular cases it may be better to go for a quicker solution. For British Telecom we are following a route which combines rapid liberalisation with privatisation (accompanied by a degree of regulation). We shall want to see how this works out in practice when considering our approach to other monopoly utilities.

6. Early consideration is therefore essential. | It must be done case-by-case. | Most of the detailed work on individual industries can only be carried out in the sponsor Departments using their knowledge of these industries, although Treasury officials will need to be closely involved. I am attaching a paper by Treasury officials which sets out some thinking about questions of competition and structure and illustrates how this could be applied in certain of the larger public sector industries, not all of which currently figure in the privatisation programme. Treasury officials will be glad to discuss these matters further with the individual sponsor Departments concerned.

7. Second, and following from this, there is now a much greater need to consider the privatisation programme as a whole. This is essential if we are to avoid potential bottlenecks in bringing a range of industries and companies to market. Bottlenecks can arise in the legislative programme, as we have seen in the plans for 1983-84 where there have been difficulties about the inclusion of



legislation relevant to privatising National Bus and British Airways. They can also arise in the capital market, where the sheer size of the bodies to be privatised can create difficulties both for other Government sales or for the private sector. This problem is raised in an early and acute form by the proposed sale of British Telecom.

8. Both these aspects point to a need to strengthen our existing procedures. We shall certainly want to have periodic reviews of progress. But we need to do this on a more systematic basis than hitherto. We need to produce for each major privatisation candidate a programme and a time-table which will map out the various issues needing to be resolved, e.g. what structural changes (if any) are to be considered; how and when this is to be done; the approximate time-scale for making such changes; the target date for privatisation; and the likely scale of the equity to be sold. I recognise that there will be uncertainties at the outset particularly about some of the later stages along the route. But in this way we can best ensure that while maintaining a worthwhile programme of asset sales we put the emphasis on maximising competition, and at the same time avoid as far as possible any potential bottlenecks in implementing the agreed programme.

9. I am therefore asking all colleagues with privatisation responsibilities to let me have by end-September a time-table of this kind for each of their candidates. John Moore, who has been given particular responsibility for privatisation within the Treasury, will then discuss these replies with sponsor Ministers in each case and subsequently report on the programme as a whole.

10. I am copying this minute to all our Cabinet colleagues and to Sir Robert Armstrong.

A handwritten signature in dark ink, appearing to be 'N.L.'.

(N.L.)

25 July 1983