PRIME MINISTER

GUANGDONG NUCLEAR POWER STATION

EX Committee is invited to agree to increasing support for GEC's bid up to 30% of the value of the conventional island.

How much support is worth giving?

As a means of protecting particular jobs, this form of support is probably the most expensive of any that we give. There is less than £200 million worth of UK manufacturing output in this project, measured at today's prices. This is equivalent to about 12,500 man years of work (half that which is claimed in the DTI paper). The level of support already agreed (22%) would imply a subsidy of £5,000 per job-year. The 30% level of support which is proposed would imply a subsidy of £7,000 per job-year, averaged over all the manufacturing jobs involved. Averaged over the 40% of the work reckoned to be undertaken in the Assisted Areas, these costs rise to £12,500 and £17,000 respectively. Many of these jobs would survive anyway so the cost per job year maintained is much higher. Regional policy, on average, involves a subsidy per job year of around £2,000-£3,000 for each additional job generated. Therefore, insofar as this project is regarded as a contribution to regional policy, it is many times more expensive than regional grants. Moreover, regional grants will already have been paid in respect to the capacity involved.

The review of regional policy has concluded that the cost per job of that policy is much too high. Surely, then, we do not wish to increase the costs of this project, which are already several times greater, and in addition to, regional support.

Looking beyond the project, the business which GEC hopes to secure as a result of its establishing a reference plant involving high-speed 1000 MW sets, could conceivably make this investment worthwhile in industrial terms. However, the likelihood is that GEC will seek subsidies for this additional business too. This is the land of the never-never: what we buy with our subsidy is the opportunity to win more orders with more subsidies. There will always be a justification - a new market, a more advanced technology, intensified competition, industrial capacity at risk.

Is there a need to make more concessions at all?

Understandably, the DTI paper overplays the case for concessions - our own technology is "weak", the French may try to ditch us as a partner; "the Hong Kong card has already been played". As to technology, it is true that we do not have a proven, high-speed 1,000 megawatt set, but neither has Alsthom Atlantique, Framatom's alternative partner. (The two competitors with established, large high-speed sets - KWU and Brown Boveri - are not in contention for this project). It would be the French, not us, who would look bad if the cooperative arrangement collapsed. Moreover it is not clear why the Chinese would wish to disappoint us at this particular delicate stage in our negotiations.

GEC's room for manoeuvre on price.

Since GEC sees this project as a strategic one to win, their willingness to negotiate on price ought surely to reflect this. GEC has the liquid assets (well over £1,000 million) to take a long view. The DTI paper comments that the GEC price is "competitive" and that it is not seeking "an excessive profit, undue recovery of overheads or reasonable contingencies".

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GEC states that their profit is £14 million on the basic contract price of £287m. A further £16m is allowed for contingencies and negotiation. DTI's financial staff judge these to be reasonable. Our conservative assessment is that £10m of this is in fact profit for GEC. In addition, GEC could press its suppliers to trim their margins. But even without doing this, GEC could, without difficulty, reduce its bid by £4m and still have £20m profit. It has the room for manoeuvre to offer most of the packages in the Annex to the paper with the support already committed by the Government, which at 22% of project cost is already double the normal rate for China (11%).

RECOMMENDATIONS

GEC are taking the Government for a ride. There is no case for any additional aid. The Government should stand on its commitment, offer GEC export financing worth £75m plus support of £4.4m (together worth 22% of the contract as it stands now), and leave it to GEC to negotiate with their own (considerable) resources.

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