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Parliament  
let JV



DEPARTMENT OF TRANSPORT  
2 MARSHAM STREET LONDON SW1P 3EB

Prime Minister (2)

The Lord Cockfield  
Secretary of State for Trade  
Department of Trade  
1 Victoria Street  
SW1H 0ET

A conundrum - but

I think the right  
4 November 1982

answer emerges.

MS 4/11

Dear Mr. ...

You, and colleagues, will recall that a year ago we agreed to a merger between the two loss making hovercraft operators Hoverlloyd (owned by a Swedish Company Brostrums) and Seaspeed (owned by British Rail). The merger had been the subject of an investigation by the Monopolies and Mergers Commission who had concluded that it should be accepted, since otherwise it seemed likely that this form of transport would disappear from the Channel.

Although both companies took a 50% shareholding in the new venture (Hoverspeed) - we agreed that to give the company the best prospect of future success it should sever its public sector links. BR therefore gave public undertakings, which I repeated to Parliament, and in contacts with the shipping industry, that they would not intervene in the management of the company, and that they had no intention of providing any additional financial support once the company was launched. As a result of these undertakings the company was recognised as being in the private sector - and sponsorship responsibility for this private ferry company passed from my Department to yours.

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Unfortunately I now hear from British Rail that the company have had a very bad first year, with a result some £5m worse than budget. A substantial part of this can be attributed to specific management failures which have been remedied and would not be repeated, and the two shareholders believe the company should be given at least one more season to prove itself. But this would require an overdraft limit of some £9m during the winter, and their bankers have said they are unwilling to go beyond the current limit of £4m without some guarantee from the shareholders.

The chances of the guarantee being called are small since the company's trading pattern is cyclical, and so if it continues to trade through the winter its financial position will then improve progressively throughout the summer. The company's current overdraft is about £2m. Brostrums have said that they would be prepared to give a guarantee, but on condition that it is matched by BR and, if called, is drawn down in parallel with BR's.

BR think it would be in their commercial interest to give the guarantee. They have a commitment to the Dover Harbour Board, and they derive appreciable extra rail income from hovercraft passengers. The BR unions would undoubtedly use the failure of this privatised company to encourage resistance to further privatisations. On the other hand, the closure of hovercraft operations would provide a substantial additional slice of traffic, which should improve the profitability of other ferry operators, including Sealink.

In the normal course such a decision could be left to the judgement of the shareholder concerned. But here the shareholder is BR, who require my consent to give any guarantee, and who did give implied commitments that they would not stand behind the borrowing of Hoverspeed. It would, I think, attack the credibility of Government statements in other privatisation

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cases - particularly those where we are retaining 51% - if BR, with our agreement, now went back on that stance of non-intervention.

I conclude therefore that in spite of the unusual circumstances we must make it clear that on a point of principle the Government is not prepared to see BR guarantee this borrowing. One would hope that the bank could be brought to see the significance of this stance in the wider context, and that they would decide whether to assist the company on its merits, without the Government/BR guarantee. But I think we will have to face a real possibility that the bank will not continue on those terms and that the company will cease trading. Whether anyone else would attempt to take over the assets and run a channel hovercraft service is difficult to predict. But the operational problems are considerable, and so we might see the end of this form of transport on this route. Moreover it may be said that this is the Government's fault since we would not even allow the public sector partner to match the private sector partner's decision.

I understand that in the next day or two British Rail will be formally requesting my approval for a guarantee. If you and other colleagues agree with the approach outlined above, I will make it clear to BR that the company must seek any support entirely from private sector sources.

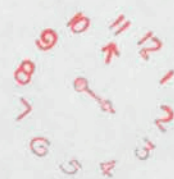
I am copying this to the Prime Minister, the Foreign Secretary, colleagues on E(EA), and to Sir Robert Armstrong and Mr Sparrow.

*Yours ever*  
*David*

DAVID HOWELL *→*

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4 NOV 1982



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Prime Minister (2)

MS 9/11

Treasury Chambers, Parliament Street, SW1P 3AG

Rt Hon David Howell MP  
Secretary of State  
Department of Transport  
2 Marsham Street  
London SW1P 3EB

9 November 1982

D Davis

mt

HOVERSPEED

I have seen a copy of your letter of 4 November to Arthur Cockfield. It is, as you say, most unfortunate that Hoverspeed have had such a bad first year and I hope that every effort can be made to encourage the interest of the banks or other investors, given the unusual position of British Rail as a parent company. I agree with you, however, that we should not allow British Rail to override the disclaimers it made and issue a guarantee. To do so would call into question the credibility of the privatisation programme as a whole.

I am copying this letter to the Prime Minister, the Foreign Secretary, members of E(EA) and to Sir Robert Armstrong and Mr Sparrow.

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LEON BRITTAN

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Presently on Parliament PM's Question in H/C July 79

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Transport

Prime Minister (2)

Ms 12/11

CABINET OFFICE  
Central Policy Review Staff

70 Whitehall, London SW1A 2AS Telephone 01-233 7765

From: John Sparrow

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Qa 06139

12 November 1982

The Rt Hon David Howell MP  
Department of Transport  
2 Marsham Street  
LONDON S W 1

Dear David,

Hoverspeed

Thank you for sending me a copy of your letter of 4 November to Arthur Cockfield.

I agree with you that the credibility of other privatisation moves would be damaged if British Rail were to give a guarantee of Hoverspeed's borrowings, and that such an unfortunate precedent should be avoided. It is, however, worth considering whether or not there are alternatives to a British Rail guarantee.

This will obviously depend on a more informed analysis of the commercial prospects of Hoverspeed than I am in a position to make, and it may be that cross-Channel services generally are in over-supply, and need to be reduced. In the private sector, some holding companies refuse as a matter of principle to guarantee their associated companies, although rarely their subsidiaries; it is nonetheless much more likely that a private sector company standing in BR's shoes would decide whether or not to guarantee simply by reference to the perceived chances of ending up with a successful (and unguaranteed) investment.

In the present case, I understand that Brostrums are prepared to guarantee the proportion of borrowings attributable to their shareholding. One possibility might therefore be for Brostrums

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(or anyone else) to be invited to make an offer for BR's shares, at a price which reflects the prospects for success. Another possibility might be for Hoverspeed to seek a third party guarantor - perhaps in the financial sector - to stand in BR's place for a fee which would presumably reflect the degree of perceived risk. There may well be other ways of meeting the problem.

In short, the Hoverspeed case raises issues of wider relevance. On the one hand, guarantees effectively from Government are damaging to the whole privatisation programme and for that reason should not be given. On the other hand, it would also be damaging if privatised companies fell by the wayside immediately after privatisation or if it appears (as the Brostrum position might indicate) that a truly viable operation is being denied support which is only temporarily required. The need therefore is to seek acceptable alternatives to the unacceptable suggestion of a guarantee.

I am sending copies of this letter to the recipients of yours.

*Yours sincerely,*

*J.S.*

John Sparrow