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For ECA meeting

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SECRETARY OF STATE
FOR
NORTHERN IRELAND

The Rt Hon Michael Heseltine MP
Secretary of State for Defence
Ministry of Defence
Main Building
Whitehall
LONDON
SW1

8 March 1985

Dear Secretary of State

RAF TRAINER

I understand that the meeting of the Equipment Policy Committee (EPC) yesterday concluded that, while both the Shorts' Tucano and BAe PC-9 planes fully meet the MOD specification and the Shorts' plane has cost advantages it would marginally favour the PC-9. My officials did not of course participate in the EPC process and I am sure that you will agree that now is the time to move to collective discussion with colleagues about the order. Before that discussion, it might be helpful to let me and colleagues have a copy of the paper considered by EPC.

It seems to me that the Shorts bid commends itself particularly well to our joint aims. As stated above it meets the specification sought by MOD and in cost terms when assessed on our agreed policy of firm prices, it gives best value for money - the hallmark of our approach to public purchasing policy.

As well as value for money there are wider arguments in favour of the Tucano which colleagues will wish to consider:-

(i) Competition

We are all agreed that fostering of greater competition amongst defence material suppliers will bring about significant public expenditure savings. I am sure that competition was responsible for the considerable reduction in prices achieved when the Trainer contenders submitted

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their "best and final" offers. Some 70% of the BAe aircraft turnover already comes from the MOD, compared with only 2% for Shorts and BAe takes the lion's share of RAF aircraft orders. But our claim of seeking to foster greater competition would suffer a considerable loss in credibility if, on this occasion when we have the opportunity to widen competition by providing Shorts with an entree into the market for RAF aircraft orders with a product that is at least the match in every way of the BAe product, we fail to do so. I think it would also be fair to say that Short's tightly knit operation with relatively low overheads geared to a commuter airline product-range is better suited to producing a small aircraft such as the Tucano.

(ii) Privatisation

The RAF contract and a successful joint venture with Embraer are critical to any decision we might make for the privatisation of Shorts; the award of the contract should make it possible to privatise the Company if Ministers agree to this course of action. The contract's importance to the forthcoming sale of BAe shares would be marginal by comparison.

(iii) Trade

In terms of export demand the Tucano is at least as attractive as the PC-9. Indeed the Tucano is already a proven success in world markets and the Short's version has an enhanced specification. The Tucano is, of course, fully compatible with the Hawk as an export package. Geoffrey Howe has, I know, already underlined to you the importance of Brazil as our largest export market in Latin America and the way in which the award of the contract to Shorts could contribute to our aim of further consolidating in that market.

(iv) Employment

The airframe of the Short's Tucano will, for both the RAF and export orders, be almost entirely built in the UK. In contrast, for the PC-9, a significant part of the airframe for the RAF order and over half of the airframe for export orders (which are likely to be considerably greater than the RAF order) will be built in Switzerland. The additional direct jobs thus created if the Tucano is successful should be a significant factor in our considerations. Comparison of indirect jobs is more difficult. The offer by Pratt and Whitney to increase the UK content of their engine is balanced by Garret's agreement with Rolls Royce offering additional UK employment if the Garrett engine is selected.

As you know, Shorts were offered grant aid on the Tucano project and I should like to clarify any misunderstanding on this matter. The

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£4.6m grant aid for the Tucano was approved by E(A) Ministers last November and is within our agreed policy of encouraging manufacturing industry in Northern Ireland. It will be funded out of the budget we have already earmarked for Shorts and will have no additional public expenditure implications.

One final point. The excellent performance by Shorts and its work-force has been well recognised in recent years by the world aerospace industry - the US Government contract to supply aircraft to the USAF, the recent order for aircraft for China, the Company's links with Boeing, and the winning of the V2500 engines nacelle contract, in the face of intense international competition. These orders signify a recognition by overseas customers of the quality of Short's products and the Trainer contract, which would fit comfortably into the Company's forward work programme, provides an excellent opportunity for HMG to give similar recognition to the Company.

We can discuss the details on these and indeed other points which colleagues will wish to raise at an E(A) meeting to which I hope Geoffrey Howe might be invited. If, as I understand, an early decision is required this is something that we might discuss at the E(A) which I understand is being planned for 20 March.

A copy of this letter goes to the Prime Minister, Members of E(A), Sir Geoffrey Howe and Sir Robert Armstrong.

Yours sincerely

J. Duill

(Private Secretary)

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(Approved by the Secretary of State
and signed in his absence)

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