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Ref. A085/854

PRIME MINISTER

A New Basic Trainer for the Royal Air Force

FLAGA — (C(85) 7)

BACKGROUND

The Secretary of State for Defence seeks endorsement of his proposal that the contract for the new Royal Air Force (RAF) Basic Trainer should be awarded to Short Brothers Limited. This course is supported by the Secretary of State for Northern Ireland; the Secretary of State for Scotland, however, would prefer the contract to go to British Aerospace (BAe). A Cabinet decision is urgently required so that it can be taken into account in the preparation of the initial Prospectus for the sale of the Government's remaining holding of BAe shares, which is scheduled for publication on 2 April.

2. The Basic Trainer will replace the existing Jet Provost. The contract will be worth about £150 million for 130 aircraft over six years: in addition there will be export orders. Four aircraft were originally considered, but two (the Westland A20 and the Hunting Firecracker) have been eliminated on technical and cost grounds. The two aircraft which remain in contention are:

- (i) the Tucano, built by Short Brothers in partnership with Embraer of Brazil; and
- (ii) the PC9, built by BAe in partnership with Pilatus of Switzerland.



MAIN ISSUE

3. The issue is whether the Cabinet should endorse Mr Heseltine's recommendation that the contract for the next RAF Basic Trainer should be placed with Short Brothers.

The Basis for Decision

4. The first question is whether a new trainer is required. The possibility of refurbishing the existing Jet Provosts had been kept open, but Mr Heseltine rejects it as more expensive in the longer run. We understand that the Treasury agree with him.

5. Given that a new aircraft is needed, the choice between the Tucano and PC9 is finely balanced. The factors to be considered are:

(i) Operational criteria. Both aircraft are acceptable in technical and performance terms. The PC9 is preferred by the RAF as its performance is closer to that of a front-line aircraft and so would make for slightly faster training of pilots.

(ii) Cost. On a firm price basis the Tucano is £6 million cheaper (£158.9 million as against £164.9 million). Even if the Government were to accept the late bid from BAE referred to in Mr Heseltine's minute of 19 March, the Tucano would still, on the same basis, be cheaper by £1.5 million. It is also cheaper to operate and this is valued, over the life of the aircraft, at £9 million.

(iii) Employment and regional development implications. The total impact on jobs (including indirect effects and

PC9 preferred
by R.A.F.

FLAG B —



commitments by the engine manufacturers to increase United Kingdom content) is estimated as

PC9

Tucano

1,302-1,352 jobs

1,158-1,208 jobs.

Within these totals the PC9 would bring 320-350 jobs to Humberside and 210-230 jobs to Scotland*, and the Tucano would bring 630-680 jobs to Northern Ireland.

*These would be at Prestwick (in Mr Younger's constituency), where the BAe establishment is mainly engaged on the successful Jetstream aircraft.

- (iv) Implications for competition policy. Shorts are the lowest tenderer, and there would need to be strong grounds for rejecting their bid. Moreover they have little RAF work at present, and giving them an entry into the market would widen the range of potential suppliers of defence aircraft, so holding out the prospect of significant public expenditure savings in future. Moreover the relatively simple Tucano is the type of aircraft Shorts generally produce, whereas BAe do relatively little work in this "lower technology" sector. On the other hand, Short's entry into this market could be seen as further exacerbating the aircraft industry's problem of world-wide over capacity, albeit in a very marginal way.
- (v) Effect on the companies. For Shorts, success is very important for their corporate strategy and could prove to be the key to a successful privatisation of the company in due course. The contract is much less significant to BAe (it corresponds to about 2 per cent of the total annual expenditure with the company by the



Ministry of Defence) but could be seen as helping market sentiment for the forthcoming sale of the Government's shareholding.

- (vi) Export potential. The best guess is that 265 PC9s could be sold abroad (BAe would get 40 per cent of the airframe work), compared with 200 of the Tucano. In terms of direct United Kingdom jobs created by exports, the Tucano has the edge. ?

P.C.9.

- (vii) Impact on foreign relations. Whichever company is chosen there will be an adverse effect in the losing country - Switzerland or Brazil. Some export orders might be put at risk. (The Lord President, who has just returned from Brazil, may wish to comment on this.)

6. Ministers will give their assessment of these factors. The Tucano appears to have the advantage on cost and on competition policy grounds, and would be fully adequate for the RAF's needs. The PC9 is a slightly better aircraft. Account will need to be taken of the industrial and regional policy implications of the choice, including those for employment in Humberside, central Scotland and Northern Ireland.

Timing of an Announcement of the Decision

7. The Secretary of State for Defence says nothing about the method and timing of an announcement of the Government's decision, but it would seem sensible for a separate announcement to be made well before publication of the BAE Prospectus on 2 April. It would be as well to establish that this is indeed Mr Heseltine's intention.*

I understand that he wishes to make a statement as

Murphy

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HANDLING

8. You will want to ask the Secretary of State for Defence to introduce his paper. The Secretaries of State for Northern Ireland and Scotland will want to speak on the regional implications of the choice, and the Secretary of State for Trade and Industry and the Foreign and Commonwealth Secretary will want to speak on the industrial trade and foreign relations aspects.

CONCLUSIONS

9. You will want to reach conclusions on:

- (i) the choice between the Tucano and the PC9; and
- (ii) the method and timing of an announcement of the decision.

RA

ROBERT ARMSTRONG

20 March 1985



10 DOWNING STREET

Prime Minister

RAF Trainer

This is the paper for
Cabinet. It deals with
the points you
wanted covered: although
the subsidy aspect appears
only in the Annex at
paragraph 7.

CDD Mr
11/3.

ACTION

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CABINET AND MINISTERIAL COMMITTEE DOCUMENTS

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