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10 DOWNING STREET

From the Private Secretary

5 August 1985

BSC STRATEGY: ANNOUNCEMENT

The Prime Minister has seen your letter to me of 2 August and, subject to the views of the Secretaries of State for Scotland and Wales, is content with the announcements to be made by BSC and your Secretary of State.

I am copying this letter to Rachel Lomax (H.M. Treasury), John Graham (Scottish Office) and Colin Williams (Welsh Office).

(Andrew Turnbull)

Miss Maureen Dodsworth,
Department of Trade and Industry.

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Secretary of State for Trade and Industry

2 August 1985

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Andrew Turnbull Esq
Private Secretary to the Prime Minister
10 Downing Street
LONDON
SW1

Prime Minister ①
Content subject to clearance
with C/IG and S/S Scotland
and Wales?

AT 2/8

Dear Andrew,

MT

BSC STRATEGY : ANNOUNCEMENT

BSC intend to make their announcement of future strategy at 11.00 am on Wednesday 7 August. I enclose a copy of their planned statement, agreed by the Board, and the draft of a statement which, as agreed by Ministers collectively, will be made by my Secretary of State endorsing the new basis for BSC's planning.

2. The announcement will no doubt attract questions about the Government's role in deciding on BSC's strategy, policy towards privatisation, and other matters. We are co-ordinating with BSC our line in response to such questions.

3. Because of the sensitivity of the Alphasteel arrangement, BSC are waiting until early next week before they inform the trade unions about the planned announcement. Sir Robert Haslam is also making arrangements to brief the Secretaries of State for Scotland and Wales on Tuesday about BSC's plans.

4. I am sending copies of this letter to Rachel Lomax (Treasury).

Yours sincerely
Maureen Dodsworth

MAUREEN DODSWORTH
Private Secretary

Press Announcement

EMBARGO: Not for publication before 11 a.m. on Wednesday, August 7th, 1985.

BSC: the Future.

British Steel Corporation Chairman, Sir Robert Haslam, today (Wednesday, August 7) announced that BSC has agreed with Government, subject to the necessary specific formal approvals from the European Commission, the basis on which the Corporation's configuration will be planned for the immediate future. It incorporates the following features:

- . An agreement reached with Alphasteel Limited, Newport, South Wales, as a part of the necessary further restructuring in the European Community steel sector, for the acquisition by BSC in 1986 of Alpha's hot strip mill.

- . The installation in Llanwern, following their acquisition from Alphasteel, of two continuous slab casting machines; and the completion of the Port Talbot hot strip mill refurbishment through the provision of a second new reheat furnace, thereby enabling the full benefits of that development scheme to be attained.

- . The closure of BSC's Lanarkshire based Gartcosh cold rolling mill and, in due course, of Alphasteel's hot strip mill, to assist the process of bringing capacity and demand more into balance in these two product sectors.

- . No intention to make investments in new coke ovens at this stage.

- . Maintaining steelmaking at BSC's five integrated steelworks sites, for at least three years from now, but subject to market demand and BSC's performance.

- . Agreement, in principle, for Government funds to support establishment of the Phoenix II business with GKN, thereby restructuring the UK engineering steels sector for the future.

These features are commented on more fully below and BSC's configuration, allowing for these measures, will be the basis on which the plan for BSC will be submitted to the European Commission.

BSC/ALPHASTEEL

The present and forecast demand and consequential substantial excess capacity for wide hot rolled coil both in the UK and in the rest of the European Community have led the European Commission to call for further significant rationalisation of existing wide hot strip mill capacity in the Community.

As part of this restructuring, ^{and} ~~which is~~ subject to the formal approval of the European Commission, BSC and Alphasteel have agreed that as from 15th January, 1986, BSC will acquire a section of Alphasteel's existing business, comprising the totality of its wide hot rolled coil/sheet operations together with the production and delivery quotas pertaining thereto.

Alphasteel is a UK limited liability company, with its works in Newport. Based on electric arc steelmaking, it currently produces and sells wide hot rolled coil, billets, and slabs. The plant which will be acquired by BSC comprises two single-strand continuous slab casters and a semi-continuous wide hot strip mill. The strip mill has a maximum capacity of over 1 million tonnes per annum, but is currently producing at a low level of capacity utilisation, *due to the extremely low quotas allocated by the European Commission.*

After modification and modernisation, BSC will install the two continuous slab casters as a twin-strand caster in its Llanwern Works, which will improve operating efficiency and enable Llanwern to meet the increasing demand on BSC for continuously cast steel qualities. It is envisaged that, in due course, the Alphasteel wide hot strip mill will be closed and sold outside the European Economic Community.

Alphasteel will retain and continue to operate its steel-making furnaces for billet and slab production for export.

Alphasteel have stated that there will be no enforced redundancy and every effort will be made for the workforce affected to continue further employment in billet and slab production.

GARTCOSH COLD MILL

BSC intends to close its cold strip rolling facility at Gartcosh in Lanarkshire on 31st March, 1986, allowing the Corporation more effectively to load its other, more modern, cold mills at Shotton, Llanwern and Port Talbot, and thereby maintaining service to customers.

The closure will improve overall cold mill productivity, reduce surplus capacity, cut overhead costs and, against limited cash resources, avoid the substantial capital investment otherwise needed at Gartcosh to improve cost competitiveness and product quality.

Ravenscraig will continue to be the main supplier of hot rolled coil to BSC's modern cold rolling and finishing plant at Shotton. As a result of the closure of Gartcosh this line of supply will be increased and, combined with supplies to BSC's tinplate plants and direct to customers, will be the main outlets for the product of the Ravenscraig hot strip mill.

This closure will result in the loss of 550 jobs at Gartcosh and 160 jobs elsewhere in the Scottish works involved in servicing the Gartcosh operation. Discussions with trade union representatives will commence immediately. The usual full counselling services will be provided at the site and every effort will be made to redeploy personnel to other BSC works and to provide assistance from BSC Industry plc.

INVESTMENT IN COKEMAKING

Coking capacity within the Corporation is adequate to support current ironmake. However, by the early 1990's there will be a deficit equivalent to some 20 per cent of estimated consumption.

A number of ways of diminishing the estimated deficit are currently being actioned:

- . Coke oven repairs - The recently developed silica welding technique has been used successfully at several of the Corporation's ageing coke oven batteries including extensive application at Ravenscraig and Llanwern. As a consequence, oven lives are being progressively extended.

- . Coal injection into blastfurnaces - Operating experience in the industry to date has shown that it should be feasible to replace 20% or more of total coke usage with crushed coal injected through the tuyeres of the blast furnace.
- . Coal injection into BOS vessels - Trials are ongoing with the objective of increasing the usage of scrap, thereby reducing iron usage in steelmaking and consequently the blast furnace coke requirement.

Until the practical potential from these developments is clearer, and because of greater investment priorities (e.g. continuous casting) and limited financial resources, the extent and timing of further coke oven investment is uncertain. It is possible that the final overall coke deficit will be too small to justify new coke oven development and purchases may prove the most economic way of providing the shortfall, particularly if the technological developments are highly successful and therefore limit world metallurgical coke demand.

STEELMAKING CAPACITY.

The Government and BSC have agreed that the Corporation should plan on the basis that steelmaking continues at all five of BSC's integrated steelworks sites for at least three years from now, subject to the market and to BSC's performance.

The closure of Alpha's hot strip mill, following its acquisition in 1986, would reduce the UK's hot strip mills from four to three. That will represent a step forward in the restructuring still required in this product area and will also help to improve the Corporation's financial position.

PHOENIX II

As stated in a joint announcement in the following terms today, British Steel Corporation and Guest, Keen and Nettlefolds plc have reached agreement in principle with the Department of Trade and Industry (DTI) on proposals for a joint venture in engineering steels, code-named Phoenix II. Clearances have still to be obtained from the European Commission and the Office of Fair Trading.

BSC and GKN will now reopen their earlier discussions with a view to the formation of a jointly-owned Company and with the objective of the new Company commencing trading by 1st April, 1986. Detailed arrangements have still to be fully developed, but the new Company will include manufacturing activities of the BSC Special Steels business and GKN's special steels and forgings operations. The forgings operation will continue to be managed and technically supported under special arrangements with GKN.

The DTI has stated that it is willing to make finance available to the joint venture through BSC and subject to finalisation and joint agreement of the detailed arrangements.

The new Company will occupy a leading position in the European engineering steels' industry and be competitive with other large European integrated steel and forging companies. The proposed merger is consistent with the European Commission's aim of achieving a restructured and strengthened Community steel industry.

Separate announcements are being made to the employees concerned and further public announcements will be made in due course.

Commenting on the announcement, the Chairman said:

'The decisions embodied in this statement represent the way ahead for BSC in the immediate future. BSC and the Government fully recognise and appreciate the efforts of the workforce and management in improving the Corporation's performance and efficiency. I am pleased, therefore, that it is now possible for BSC to make further progress through the understanding and helpful co-operation of Alphasteel in reaching agreement with us on their hot strip mill operations.

"Nevertheless, decisions on the longer term future will depend on market developments and BSC's ongoing performance, and it is vital for the Corporation to avoid new borrowing in the face of the modest growth for the steel industry and the Community as a whole, foreseen by both BSC and the European Commission. In this situation, the key question is whether, in fact, there will be sufficient good margin business to enable BSC to achieve fuller utilisation of our potential capacity, and thereby generate sufficient cash from profits to renew and continuously to modernise our equipment. Only through doing this can we maintain the core of BSC's business in a fully competitive state whilst providing customers with competitively based products. The Corporation continues in its belief that it remains to be seen whether the steps now being announced will be sufficient to meet these objectives."

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The Secretary of State for Trade and Industry, commenting on Sir Robert Haslam's statement, said that the decisions announced by BSC had been taken after consultation with the Government and represented a strategy agreed between BSC and the Government for the next three years.

The Secretary of State for Trade and Industry said "The Government's objective is that BSC should be restored to commercial viability and, eventually, privatised. I welcome the establishment of an agreed planning basis for the next three years which will put BSC on course to meet these objectives. In particular, I welcome the prospect of a further significant privatisation of BSC in the area of overlap between the Corporation and the private sector. While regretting the loss of jobs which result from the decision to close Gartcosh, the Government accepts that this decision is properly a matter for BSC management to take, and is compatible with the agreed strategy.

From the Government's point of view, the essential feature of the agreed strategy is that, barring unforeseen changes in underlying market conditions, steelmaking will continue at all five of BSC's main integrated sites for at least the next three years. It is simply not possible to see further ahead than that in the present uncertain market. Within this framework, BSC will continue to be free to take management action to cut costs where necessary.

I join with Sir Robert Haslam in recognising the efforts of BSC's workforce at all levels from shop floor to Boardroom in improving the Corporation's performance and efficiency. The agreement with Alphasteel Ltd will enable the Corporation to make further improvements in its performance, and produce a plan which I am confident will demonstrate its viability.

The decisions announced today cannot, however, mean that any particular works or plant is permanently safe. The steel industry is subject to risk, and the future of BSC's plants will depend on future market developments, on their being operated to the highest efficiencies, and on the Corporation's overall financial performance. In particular, if the Community agrees, as we hope it will, on a ban on extensive state aid after 1985 to eliminate unfair competition any major and sustained shortfall in BSC's financial performance would require prompt corrective action.

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Background

BSC planning since 1982 has been on the basis of the Government statement of 20 December 1982, when the Government asked BSC to prepare its plan for the next three years on the basis that steelmaking would continue at all five major integrated sites. BSC accepted the aim of breaking even before interest in 1984/85, and it remained free to take management action to cut costs where necessary in order to maintain efficient operations and to move steadily towards the objective of viability. But for the miners' strike, BSC would have made a profit after interest in 1984/5, and the Corporation is currently trading profitably. The Government expects it to earn a profit after interest in 1985/86.

It is now the third year of the three year plan produced by BSC on the basis of the Government's 1982 announcement. Last year, BSC's planning process was interrupted by the miners's strike, and it has only been with the ending of the dispute and the resumption of normal trading and supply conditions that BSC and the Government have been able to discuss future strategy.

In addition, the EC rules on state aids for the steel industry mean that BSC has to draw up a plan this year demonstrating its viability in 1986 and beyond. Approval by the Commission of the BSC plan is necessary to enable the Government to pay the remainder of the aid BSC requires this year, and to enable BSC's external finance needs after 1985 to be seen as not involving further subsidy. The BSC plan is being prepared on the basis that steelmaking will continue at all five main integrated sites or at least the next three years, barring very radical unforeseen changes in underlying market conditions. (The Government is confident that, taking into account the effects of the decisions announced by BSC today, the plan will demonstrate BSC's future viability).

The Community steel regime exerts a major influence on conditions in the European steel market. The period since 1982 has seen some recovery in the performance and prospects of the European steel industry, helped by the Community's anti-crisis measures. Considerable progress has been made in removing excess capacity throughout the Community, and by the end of this year, more than 30 million tonnes of capacity will have been shut since 1980. But the Commission estimate that a further 20 million tonnes will need to close over the next few years if the Community industry as a whole is to become securely viable.

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Against this background of considerable but incomplete progress in solving the problem of overcapacity, the Council of Ministers agreed on 25 July that the Community's market organisation measures should continue for a further period of up to 3 years, but modified in ways to permit a smooth transition back to a free market by the end of this period. This should help to sustain market stability in the face of continued overcapacity. In addition, the Council of Ministers will need to decide later this year what limited, if any, state aids should be permitted for the steel industry after expiry of the present regime at the end of 1985. The Government intends to pay no further subsidies to BSC after that date, and regards it as essential that the Community should not permit payment of extensive state aids by other member states which could disadvantage the BSC and UK private sector steelmakers.

The decisions announced by BSC concerning the closure of Gartcosh and future investment in coke ovens do not concern matters which are subject to specific Government approval, but the Government have been aware of BSC's intentions as part of the overall review of strategy. While regretting the loss of jobs resulting from the Gartcosh closure, the Government believes that the decisions are properly matters for BSC's judgment, and that BSC has taken them only after very careful consideration. The Government is satisfied that the decisions announced are compatible with the agreed strategy.

The Government have agreed in principle that Phoenix II, BSCs and GKN's joint venture in engineering steels, should go ahead. Further work remains to be done before the new company can be in operation.

The financial consequence of these decisions will be reflected in External Financing Limits for BSC to be announced later this year. They will result in BSC earning a profit after interest this year, and increasing profits thereafter.