

E(81)13

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## CABINET

## MINISTERIAL COMMITTEE ON ECONOMIC STRATEGY

## BRITISH STEEL CORPORATION: CORPORATE PLAN

Memorandum by the Secretary of State for Industry

I circulated as E(81)11 the report of officials on the BSC Corporate Plan. We now have to decide whether, as officials recommend, we should approve the Plan; and if we do what conditions, if any, we should attach to it.

The Plan

2 The Plan very much reflects Mr MacGregor's approach to his job. It is not a conventional medium-term plan looking 3 or 5 years ahead. Instead it sets short-term targets which will enable the Corporation to assess within the next 6 months which of its businesses have a reasonable chance of commercial viability by March 1982. The Plan proposes some closures but the level of production which it envisages, at 14.4 million liquid tonnes per annum (MLTA), is above the 12½-13 MLTA which Mr MacGregor indicated as his preferred option in September and which we discussed in September at E(80)34th.

3 The Plan envisages that by a combination of cost cutting and vigorous marketing the Corporation will, by the end of 1981/2, have substantially reduced the rate of loss (estimated for 1980/1 at £480m). They are asking the Government to provide money as follows:-

- (a) an extra £150m in 1980/1 to bring the total EFL to £1,121m (including £121m carried forward from 1979/80).
- (b) £730m in 1981/2.

Assessment of the Plan

4 It is clear from the report of officials that the major risk to the Plan arises from external economic factors, in particular the extent and timing of an up-turn in steel ordering in the UK, the level of the Deutschmark and the maintenance from July of arrangements to stabilise the European

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steel market. In the light of these risks, the plan to maintain capacity of 14.4 MLTA looks distinctly optimistic. Indeed, Mr MacGregor himself so characterises it. He has made a good start with the cost reductions that he needs. He has so far obtained the co-operation of the work-force in most areas and the results of the management's and ISCO's ballots indicate good prospects for its continuance. He has, however, consistently made it clear, both to Ministers and to his work-force, that if performance or the market prospects of particular parts of the Corporation do not justify their retention he will close them. What Mr MacGregor is in effect asking for is time to bring about the cost reductions that he has in mind and thus to improve the chances of viability of a larger part of the Corporation. If the market does not improve, or if Mr MacGregor cannot get the cost improvements he seeks, he will face the prospect of further major closures or reductions. In that case it is my view that we should not interfere in those decisions, though we may have to act to mitigate their social consequences.

5 We have so far adopted a stance which supports Mr MacGregor's policies. In particular, as agreed at E(80)24th and 45th, we shall shortly be publishing a Bill which, in order to help the drive towards commercial viability, writes down the capital of the Corporation but which, on the other hand, recognises the possibility of failure and proposes changes to the Iron and Steel Act 1975 to enable a rapid and extensive run-down of the Corporation to take place.

6 We have to take our decision also against the background of a private sector running increasingly into financial difficulties and complaining that the Government is biased against them and unduly soft towards BSC. For example, Dupont with a steel making plant at Llanelli and rolling mills in the Midlands are expected shortly to be put into receivership by their bankers; Lonrho cannot long keep open their subsidiary Hadfields with its plants at Sheffield. Colleagues will remember that at E(80)43rd we authorised BSC to enter into negotiations with private sector companies to see whether in areas where their activities overlapped there could be formed joint companies which would be in the private sector and whose formation would be accompanied by an agreed plan of closures. Two such companies are in process of negotiation, one involved in rod and bar manufacture (Phoenix I) and the other (and larger) in engineering steels. The negotiations on Phoenix I are well advanced and we have pressed BSC and GEM, who are the private sector company involved, to reach agreement in principle quickly so that it can be announced before our own response to the Plan.

7 It will be apparent from what I have said that, even if we back Mr MacGregor's Plan now, we may still face an extensive run-down of BSC's operations later. The costs of a run-down, whether decided on now or later, might not differ greatly;

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indeed the figure in July may be somewhat lower since at least some of BSC's operations that are not competitive now may become so as a result of the manpower and other cost reductions undertaken in the interim. If it were decided later, there would, however, be the cost of funding the BSC's operations in the interim. While in practice any such run-down would be spread over a period of time, officials have attempted to calculate, for the purpose of illustration, the approximate additional cost of delaying such a decision for six months. They put a figure to it of between £350m and £450m. They suggest, and I agree, that this is very much an outside figure since it ignores the fact that at least some of BSC operations are viable now and the possibility of interim improvements I have just referred to.

8 In these circumstances, I think we should back Mr MacGregor's commercial judgement. This has the considerable tactical advantage that if in the end BSC does have to be substantially run down, both we and the Corporation will be seen to have made every effort to make a go of it. I am also influenced very much by the fact that the Plan does not imply a long-term commitment to the Corporation in its present form, that it contains no new major capital investment programme, that there are negotiations in progress aimed at privatisation, and that Mr MacGregor is publicly committed to closing operations which cannot be made viable. All this sharply distinguishes the issue we face from that in the case of British Leyland. I therefore recommend that subject to certain points which I discuss below we should approve BSC's Corporate Plan.

#### Consequential Points

9 If colleagues accept this view we should clearly do what we can to ensure that the Corporation in practice take the necessary action should they fail to meet the targets in the Plan. With this in view, I think we should set BSC, and announce, a loss limit before interest for 1981/2 of £225m. This figure is £50m higher than that included in the Plan and recommended by officials since BSC now take the view that it is unrealistic to accommodate even a modest pay award within their original figure. I agree with officials' recommendation that we should also set, and announce, a target for 1982/3 of break-even. Mr MacGregor's own performance, upon which payments for his services depend, is linked to the attainment of profit targets.

10 I recommend also that we accept the recommendations made in the report of officials, that the Corporation should not embark on any major new capital investment project without prior governmental approval, that we should set up arrangements for monitoring BSC's progress towards achieving their targets, and that we should ask Mr MacGregor to report back to us in July. I also agree that questions of redundancy payment and Companies Act structure should, as recommended by officials,

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be discussed further with BSC.

11 The Iron and Steel Bill to give effect to the financial arrangements comes before L Committee on 4 February. It contains the statutory support we need for the policy I am recommending, as described in para 5 above. When the Committee last considered the policy of the Bill (E(80)44th and 45th) this was on the basis of notional figures for the capital write-off. The Bill in fact proposes to write-off £3509m of capital immediately with a power to write-off further £1,000m later. There are also adjustments to a Corporation's borrowing limit. I recommend that we approve these figures and that the Bill be published simultaneously with the statement announcing our decision on the Plan. In presenting it we shall of course need to emphasize the distinction between writing off the past and our future policy towards funding the BSC.

12 One of the most critical factors in the success of the Plan will be the need for continued discipline in the ECSC market for steel after the present regime expires in June. The Government will need to make strong efforts to this end, though we need to be careful to avoid a regime which results in British steel users having to pay higher prices for steel than their EC competitors. This will entail considerable ministerial effort and probably the exertion of political pressure on our EC partners. Independently of this it will also be necessary to obtain clearance from the Commission under the terms of an ECSC Decision on State Aids for Steel for the further finance we propose.

13 If colleagues agree that we support the BSC Plan it would be neatest to make a statement on Monday, 9 February when I am first at Question Time and already face a number of questions on BSC's affairs.

#### Conclusion

14 I invite my colleagues to agree:

- 1 to the approval of the BSC Plan;
- 2 to the provision of an extra £150m to BSC in 1980/1 and the setting of EFL for 1981/2 of £730m;
- 3 to the setting of a loss limit for BSC of £225m in 1981/2 and of break-even for 1982/3;
- 4 to the approval of the amounts to be written off in the Iron and Steel Bill;
- 5 that we should give strong support in the EC to efforts to maintain an orderly steel market in Europe when the present measures expire at the end of June; and

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- 6 that I should make a statement in the House of Commons on 9 February and simultaneously publish the Iron and Steel Bill 1981.

K J

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