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E(81) 5th Meeting

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CABINET

MINISTERIAL COMMITTEE ON ECONOMIC STRATEGY

MINUTES of a Meeting held at
10 Downing Street on
TUESDAY 3 FEBRUARY 1981 at 4.30 pm

PRESENT

The Rt Hon Margaret Thatcher MP
Prime Minister

The Rt Hon William Whitelaw MP
Secretary of State for the
Home Department

The Rt Hon Lord Carrington
Secretary of State for Foreign
and Commonwealth Affairs

The Rt Hon Sir Geoffrey Howe QC MP
Chancellor of the Exchequer
(Item 1)

The Rt Hon Sir Keith Joseph MP
Secretary of State for Industry

The Rt Hon Lord Soames
Lord President of the Council

The Rt Hon James Prior MP
Secretary of State for Employment

The Rt Hon Michael Heseltine MP
Secretary of State for the
Environment

The Rt Hon John Biffen MP
Secretary of State for Trade

The Rt Hon David Howell MP
Secretary of State for Energy

The Rt Hon Leon Brittan QC MP
Chief Secretary
Treasury

THE FOLLOWING WERE ALSO PRESENT

The Rt Hon Nicholas Edwards MP
Secretary of State for Wales
(Item 1)

Mr Kenneth Baker MP
Minister of State
Department of Industry
(Item 2)

Earl of Mansfield
Minister of State
Scottish Office
(Item 1)

Mr J R Ibbs
Central Policy Review Staff

SECRETARIAT

Sir Robert Armstrong
Mr P Le Cheminant
Mr D J L Moore

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1. BRITISH STEEL CORPORATION: CORPORATE PLAN

The Committee considered memoranda by the Secretary of State for Industry (E(81) 11 and 13) and by the Central Policy Review Staff (CPRS) (E(81) 14) on the British Steel Corporation's (BSC) Corporate Plan.

THE SECRETARY OF STATE FOR INDUSTRY said that Mr MacGregor, the Chairman of BSC, had put forward not a medium term Plan with options but short term targets to enable the Corporation to assess by July which of its businesses had a reasonable chance of commercial viability by March 1982. The Plan assumed a level of production of 14.4 million liquid tonnes per annum compared with the 12½-13 mta which had been Mr MacGregor's preferred option in September. Mr MacGregor acknowledged that this capacity assumption was likely to prove optimistic. He had so far been successful in winning the co-operation of the workforce and there was a reasonable chance that the Corporation could meet its objectives for cutting costs and improving productivity. It was, however, quite possible that, because of external factors, they would be unable to meet their objectives for sales and profitability. The Deutschemark, which was the main determinant of their competitiveness with European steel producers, currently stood at 5.0 to the £ compared with the average in 1981-82 of 4.2 which BSC had assumed in their Plan, and this could have a major impact on their profitability. Their sales prospects would turn crucially on the extent and timing of a revival of steel orders in the United Kingdom and on the maintenance after June 1981 of arrangements to stabilize the European steel market. If, however, BSC did not meet the objectives in their Plan, for either internal or external reasons, Mr MacGregor proposed to close those businesses which could not be made viable; and he would report progress on this to Ministers in July. To ensure that BSC took the necessary action, should they fail to meet the targets in their Plan, the Secretary of State for Industry recommended that he should now announce that the Government had set the Corporation financial targets of a loss limit before interest of £225 million in 1981-82, and of break-even in 1982-83. At the same time the External Financing Limit (EFL) for 1980-81 should be increased by £150 million to a total of £1,121 million, and that for 1981-82 set at £730 million. BSC were assuming a wage freeze in the first six months of 1981 followed

by a 7 per cent increase in July, and the financial target and EFL allowed for the £50 million cost of this in 1981-82. The Committee had already agreed that the Iron and Steel Bill should provide for capital reconstruction of the Corporation, and he now recommended that the Bill should write-off £3,509 million of capital immediately and include a power to write-off a further £1,000 million later. If the Committee approved his recommendations he would announce the Government's response to BSC's Plan, and publish the Iron and Steel Bill, on Monday 9 February. In the meantime discussions on joint ventures between BSC and private sector steel firms were continuing. It was likely that BSC and Guest Keen and Nettlefold Limited would be able to announce agreement within the next few weeks on Phoenix I, involving rod and bar manufacture, and that later they would conclude an agreement on Phoenix II for engineering steels. It was likely, however, that certain other private sector steel companies would go into receivership or be closed shortly.

MR IBBS said that the CPRS were concerned that there was a distinct risk that BSC would achieve their cost reduction and market targets but would still be losing heavily on profit targets because of the external factors, particularly the level of the Deutschemark, to which the Secretary of State for Industry had drawn attention. Although publicly the Government should now support Mr MacGregor, and the necessity of plant closures if planned targets were not achieved, there was a case for Ministers considering before July whether there were any wider considerations on which they would wish to guide Mr MacGregor privately. It would be better to do this than to face the necessity of overriding publicly, on wider grounds of policy, particular closure decisions which Mr MacGregor might feel impelled to take. Ministers might therefore wish to consider now whether there was a strategic need to retain any part of the steel industry, either to support United Kingdom customers or to ensure security of supply; and how to assess the longer term viability of plant which failed to meet short term targets solely for external reasons which might be temporary. If, following such an assessment, ground rules could be agreed with Mr MacGregor, this would prepare the way for considered judgements on the proposals which BSC would be putting forward in July.

In discussion the following points were made -

- a. The BSC's Plan offered a short-term sketch with no clear indication of how massive sums of Government money would be spent or of medium term prospects and options. If it were accepted without qualification, the danger was that Mr MacGregor might put forward further short-term proposals in July, on which Ministers would have little opportunity in practice to take a considered judgement. To avoid this, ground rules should be laid down now, on the lines proposed by the CPRS. These should include the identification of performance aims so that a judgement could be made on the extent to which the Corporation's performance was the outcome of those factors within their own control or of external factors such as the level of the Deutschemark. Against the possibility that Mr MacGregor would recommend closure of major plants, an evaluation should be made now of the wider economic and social consequences of such closures.
- b. The risk of this approach was that it implied that profitability was not to be a governing criteria in determining the future of BSC. If in practice the Government were to continue to subsidize BSC, irrespective of their success in the market and their profitability, this could be far more expensive than accepting the clear and rigorous test of profitability.
- c. If BSC were to be financed to the extent of the proposed EFLs, the private sector steel firms, some of which were now facing closure, would be highly critical of the Government. It was questionable whether the EFLs and financial targets should be increased to accommodate the £50 million cost in 1981-82 of the proposed 7 per cent wage increase from July.
- d. On the other hand, negotiation of a 7 per cent wage increase from July represented a satisfactory outcome for BSC's management. It should be seen in the context of a wage-freeze in the first six months of the year and of the reductions in BSC's total manpower from about 182,000 in October 1979 to a forecast of 125,000 at the

end of March 1981 and 108,000 a year later. At the same time considerable productivity improvements had been achieved, and productivity at Port Talbot and Llanwern was now as good or better as that in the plants of any of BSC's overseas competitors. The Corporation were much more open to criticism on the grounds that their redundancy payments were unduly generous, and they should now give notice that they did not intend to continue to pay them at this level for more than another year.

e. There was a risk that a firm target of break-even for 1982-83 would be criticised by the public as implausible. In view of the uncertainties it might be better to express this as an aim rather than a firm target.

THE PRIME MINISTER, summing up the discussion, said that the Committee agreed with the proposed provision in the Iron and Steel Bill for the writing-off of capital in respect of past losses. Before taking any decisions on EFLs, however, they wished to know in more detail how the proposed increase of £150 million in 1980-81 and the total of £750 million in 1981-82 would be spent. Further consideration should be given to requiring BSC to accommodate the costs of any wage increases this year within lower EFLs and profit and loss targets for 1981-82. The announcement of these figures, and of the Government's response to the Plan, was likely to be criticised, particularly by private sector steel firms facing closure. The Secretary of State for Industry should therefore bring out in his statement the recent achievements of BSC, in particular the substantial reductions in manpower and improvements in productivity at some plants, and, if possible, he should indicate that the present high level of redundancy payments would not be maintained for more than another year. The Secretary of State for Industry should also arrange for his Department, in consultation with the CPRS, to consider further the proposals in paragraph 6 of the CPRS's memorandum (E(81) 14), and the identification of performance targets which would enable Ministers to distinguish between the effect of internal and external factors on the Corporation's achievements. They recognised that the Secretary of State for Industry feared that any departure from the criterion of profitability would prove to be more expensive, and

could be unacceptable to the Chairman of the Corporation. They agreed, nevertheless, that further contingency planning and the establishment of clearer performance criteria were essential in preparation for the difficult decisions on the future on the Corporation with which they could be faced later in the year.

The Committee -

1. Agreed that the Iron and Steel Bill should provide for the writing-off of £3,509 million of the British Steel Corporation's capital immediately, with a power to write-off a further £1,000 million later.

2. Invited the Secretary of State for Industry to circulate -

i. a note indicating in as much detail as possible the progress for which the proposed increase of £150 million in the British Steel Corporation's External Financing Limit for 1980-81, and the total of the proposed External Financing Limit for 1981-82, were required; and whether any wage increase in 1981 could be accommodated within a lower External Financing Limit and financial target for 1981-82 than he had proposed in his memorandum E(81) 13.

ii. A draft statement taking account of the points made in their discussion.

3. Invited the Secretary of State for Industry to arrange for his Department, in consultation with the Treasury and the Central Policy Review Staff, to consider further the recommendations in paragraph 6 of E(81) 14, the points made in discussion on the identification of performance aims, and the evaluation of the wider social and economic costs of major closures, and to report.

2. INTERNATIONAL COMPUTERS LIMITED

THE MINISTER OF STATE, DEPARTMENT OF INDUSTRY, informed the Committee that the Chairman of International Computers Limited had reported, at the Annual General Meeting (AGM) earlier in the day that, while the Company was currently trading at a loss, he hoped to see improvements as the market revived and as a result of substantial measures in hand to reduce costs and to increase deliveries. The AGM had approved a special resolution raising the Company's borrowing limit. The situation did not require any decisions by the Government.

The Committee -

Took note.

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4 February 1981

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MINISTERIAL COMMITTEE ON ECONOMIC STRATEGY

Meeting held at 10 Downing Street on
Tuesday 3 February 1981 at 4.30 pm

INTERNATIONAL COMPUTERS LIMITED

The Committee had before them a minute of 2 February to the Prime Minister from the Minister of State, Department of Industry (Mr Baker) about the future of International Computers Limited (ICL).

THE MINISTER OF STATE, DEPARTMENT OF INDUSTRY, said that the financial performance of ICL had deteriorated rapidly and the Chairman had reported at the Annual General Meeting that day a pre-tax loss in excess of £20 million for the first quarter of their current financial year. The AGM had, however, approved a special resolution to enable the company to borrow up to three times its net worth rather than twice as previously. Provided that the banks were willing to increase their lending, this should enable the company to deal with their increasing borrowing requirements which were likely to reach a peak of around £180 million next August. The immediate pressure on the Company, which he had reported in his minute of 2 February, had therefore been eased. He expected that they would, nevertheless, still ask the Government to advance £70 million grants in support of research and development over the next two years. He would not accept any such proposal at this stage. The Board of ICL had now formally accepted that the company could not continue in the computer business in its present independent form. There were no prospects of purchase by, or partnership with, another United Kingdom company, and the Board were actively considering the possibility of partnerships with either Sperry Univac of the United States of America or with the Japanese firms Hitachi or Fujitsu. It was essential that any such partnership should provide for continuing services to ICL's present customers, including Government Departments and other parts of the public sector.

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THE PRIME MINISTER, summing up a short discussion, said that, principally because of the number of ICL's computers in use in the public sector, the Government had a proper concern in the future of the company, but they were no longer shareholders, and should not become more closely involved. The Minister of State, Department of Industry, should encourage ICL to pursue vigorously the possibility of partnership with another company, in a way which would safeguard the interests of existing customers both in the public sector and elsewhere. He should not, however, hold out any hope that the Government would advance further sums, in support of research and development or in any other way, and he should leave to the shareholders and the banks the question of the future of the company's top management.

The Committee -

Took note.

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4 February 1981

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