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CABINET
MINISTERIAL COMMITTEE ON ECONOMIC STRATEGY

NCB FINANCES

MEMORANDUM BY THE CHIEF SECRETARY

I recognise the importance of avoiding further confrontation with the NUM. But the proposals of the Secretary of State for Energy in E(81) 57 for the NCB's EFL and capital approval represent an extremely generous package. It goes beyond what we can properly afford and I suggest that it should be modified in the following ways.

Capital Approval

2. The Secretary of State proposes that the NCB's investment for 1981-82 should be approved at £825m compared to the "existing approval" of £765m indicated in Annex A of his paper. I recommend that expenditure should be kept at the "existing approval" of £765m and that the saving should be achieved by cutting back or deferring expenditure on new capacity. It makes no sense to invest in new capacity, however low cost the coal produced, when, as the Secretary of State recognises, the prospects are for the NCB's production to outrun UK demand for coal to 1990. Investment in new low cost capacity can only be justified by the acceptance of closure of the old high cost capacity. The industry has shown that it is not ready for this.

The EFL

3. The present EFL is £886m. Any increase represents a charge on the Contingency Reserve which is already under pressure this year.

The Secretary of State's proposal for an EFL of £1,200m would mean a charge of £314m (in cash) on the Reserve. I consider this excessive and propose an EFL of £1,100m, reducing the charge to £214m. It should be left to the NCB to decide how to keep within this EFL, but the following suggests the scope for reductions:

- i) Capital Investment: a reduction of £60m as indicated in paragraph 2 above.
- ii) Export Sales: unless the NCB can demonstrate that the port etc facilities are not available, they should aim to increase export sales still further, even if this requires sales at even lower prices.
- iii) Reduced Production at Continuing Pits: a cut in production larger than the 2½m tonnes assumed in paragraph 3(iv) of Annex B of E(81) would produce savings in addition to the £50m indicated there.
- iv) Improvements in Efficiency and Cost Saving: ^{eg} savings could be achieved through a reduction in the Board's stocks of stores. They have consistently said that they intend to do this, but have not yet produced evidence of significant savings.

The Grant Scheme

4. I agree that there should be a single new grant to replace specific operating grants and deficit grant. But I strongly disagree that this grant should "be paid before profit and loss have been struck". This presentation would give the NCB statutory backing for claiming in public that they had "broken even" despite the reality of losses of hundreds of millions of pounds. This would give a false impression of the state of the NCB's finances and make harder the essential task of mobilising public opinion in favour of action to reduce the Board's losses. I recommend that grant should be payable "after profit and loss have been struck".

Interest Remission

5. I agree in principle with the proposal in paragraph 6 of Annex C that arrangements for the deferred interest loans should permit the deferment of repayments of principal as well as interest, though the Treasury would need to consider the detailed arrangements. But I do not agree that deferred payments of interest should not be reflected in a reduced EFL. The procedure envisaged appears to be for the EFL to be fixed on the assumption that none of the NCB's loans were of the deferred interest type. If subsequently such loans were agreed, the Board's interest bill would be reduced; and the Board would be permitted to use the leeway thereby created within their EFL for additional expenditure on whatever they chose, eg wages. This is tantamount to an increase in the EFL and would increase public expenditure. The sums involved build up rapidly from about £10m in 1981-82 to £60m in 1983-84, increasing by £25m per annum thereafter for the next few years.

Recommendation

6. I recommend that:

- i) the NCB's capital approval should be £765m;
- ii) the EFL should be £1,100m;
- iii) there should be a single new grant to replace specific operating and deficit grant. But the single new grant should be paid after profit and loss have been struck;
- iv) subject to Treasury agreement on the details, deferred interest loans should permit the deferment of repayments of principal as well as of interest. But payments of interest deferred should count against the Board's EFL and the EFL reduced accordingly.