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30 June 1988

Dear John,

TYPE 23 FRIGATES

I have now considered the results of the competition for the order of the next batch of Type 23 frigates. The Type 23 is the Royal Navy's new anti-submarine frigate. The first of class, HMS NORFOLK (23-01), is being built by Yarrow Shipbuilders Limited (YSL); Swan Hunter Shipbuilders Limited (SHS) are building Type 23-02 and two others are under construction at YSL.

Tenders were invited in September 1987 from YSL, SHS, the VSEL subsidiary Cammell Laird (CL) and Vosper Thornycroft (VT) for the order of combinations of up to four more ships. The competition was hard fought, and good prices were achieved. YSL offered the best prices for three or four ships, with CL close behind. SHS were significantly more expensive for all combinations of one to four vessels, while the VT tender covered only a pair of ships and was priced well in excess of the others. There is a considerable cost advantage in placing all ships in a batch with one shipbuilder; to split a four-ship order between two yards, for example, would add at least £11M to our costs, and to divide it between three yards would add £23M.

The Rt Hon John Major MP



On the basis of value for money, there are strong grounds for ordering four ships now from YSL; the prices currently on offer may not be repeated in subsequent competitions and the addition of a fourth ship lowers the unit cost of all four by £1M per ship. Ordering four would also demonstrate in the best possible way our continuing commitment to maintain a frigate and destroyer force of "about 50", a point on which I am coming under increasing pressure in the House and upon which the HCDC has recently commented in its report on the size and role of the surface fleet. The reality is that, even if all these ships are ordered, the frigate force will consist of no more than 47 hulls in the longer term.

But the outcome of PES 87 left me with insufficient funds to order a fourth ship now. Were the fourth ship to be deleted from the programme, the frigate force level would fall to 46. This would have serious effects on the ability of the Royal Navy to carry out its peacetime and wartime tasks and would call into question the continuing validity of our "about 50" policy. As you know, I am therefore seeking additional funds in PES 88 to cover this and other important items.

Against this background, I propose to order only three ships now from YSL. To preserve our flexibility pending the outcome of PES 88, and to avoid political difficulty with our own supporters over the "about 50" policy, I would need to be able to make it clear that the fourth ship will be included in the next batch competition, tenders for which will be invited early next year (without, however, committing us to the ultimate size of the next order). This approach may also be welcomed by the unsuccessful shipyards as giving them a second chance to win the order for one of the current batch. In presenting this position, I will need to emphasise that our plans for the size of the frigate force have not changed and that the decision to order three ships at this stage reflects a balance between the



advantages of batch ordering on the one hand and the need sensibly to limit forward commitment of the defence budget on the other.

The total estimated cost of the three ships which I propose to place with YSL is £344M, including their weapons systems and equipments. The value of the order to YSL would be £157M. The order should enable YSL to maintain its workforce without further redundancies. Taking into account Trident sub-contract work from Barrow, we assess that CL should be able to sustain their present workforce until after the peak of Trident work in 1991, although the company have said that there will be redundancies if they do not win the order. Redundancies are likely at SHS, but we believe the firm will be able to survive until the next round of naval ship orders. There are few implications for VT, whose total workforce is presently engaged on the minehunter programme. It remains the case, as noted in the 1986 study on warshipbuilding capacity (E(A)(86)31 dated 24th June 1986) that the strategic requirement for warshipbuilding can be met by VSEL, YSL and VT. There are no defence reasons for splitting the order. To do so would cost the Defence Budget a premium of at least £11M, which, given the pressures, I cannot contemplate. In any case, we must sustain our competition policy.

I should be grateful for your agreement that I should proceed to place these orders now; subject to any views that colleagues may have, I hope to be able to announce them by means of an oral statement in the House as soon as possible.

I am sending copies of this letter to the Prime Minister and, for information, to other members of E(A) and to Sir Robin Butler.

Yours ever,
George
George Younger

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