

P.01069

PRIME MINISTER  

---

British Shipbuilders

E(NI)(83)15

## BACKGROUND

In this memorandum the Secretary of State for Trade and Industry sets out his proposals for British Shipbuilders (BS) in the light of the Sub-Committee's previous discussions of the industry, BS's 1983 Corporate Plan, and the present prospective market conditions for shipbuilding and BS's other activities.

2. The main figures are clearly set out in the memorandum. But you will note that there has been a significant further worsening since the Sub-Committee's last discussion of BS (E(NI)(83)2nd Meeting, Item 1). Losses in 1982-83 were £117 million, compared with the previous estimate of £57 million (and the target of £10 million). BS have applied for 'crisis aid' on merchant shipbuilding, and recognise that offshore business will be much less than their previous estimate. They have recently announced that about 9,000 jobs are likely to be lost.

## MAIN ISSUES

3. You will want the Sub-Committee to look at the Secretary of State's proposals for all of BS's divisions; but the meeting's main concern will be with merchant shipbuilding and offshore work, the Corporation's main loss makers.

Merchant Shipbuilding and Offshore Work: the proposals

4. Following E(NI)'s earlier discussion, BS were told to include in their 1983 corporate plan realistic options for reducing losses on merchant shipbuilding. Mr Parkinson reports that the Corporate Plan produced fails to do so, and argues that the Government should reject its proposals for merchant shipbuilding. His own proposals are as follows.

- (i) The new Chairman, Mr Graham Day, should be invited to produce in the Autumn a plan for a controlled run down of merchant shipbuilding.

(ii) The Government should pay 'crisis aid' of up to £100 million (instead of the £45 million planned at present) to secure orders for the potentially viable yards in 1983-84 and 1984-85. The aid might best be paid in the form of increased Intervention Fund support. 'Soft credit' might also be necessary, but any proposal for such assistance would have to be decided by Ministers collectively, as at present.

(iii) The Government should immediately begin negotiations with the European Commission to seek their agreement to the payment of 'crisis aid'.

5. On offshore work BS's corporate plan envisages that Scott Lithgow (on the Clyde) will run down and probably close, leaving Cammell Laird as the only offshore yard. Mr Parkinson concurs in this view, noting that no decision need be announced until nearer the time when the yard's present workload is completed, probably in 1985.

General approach

6. E(NI) accepted in previous discussions that substantial yard closures and redundancies would be necessary to reduce BS's losses and give the Corporation a chance of breaking even. BS's recent performance certainly gives no cause for greater optimism. The proposals in E(NI)(83)15 probably imply the closure of around half a dozen yards and a fall in merchant shipbuilding manpower to around 9,000 (17,300 at present; 13,600 after redundancies planned at present). The PSBR cost of the proposals is estimated to be £300 million over the public expenditure planning period, (compared with £335 million for BS's preferred option and £380 million for complete closure).

hag B →

7. We understand that Treasury Ministers are being briefed to support these proposals, on the grounds that they constitute a realistic attempt to get rid of yards with poor performance and few prospects; and to let BS concentrate orders and management resources on those yards (eg. Govan, Austin and Pickersgill) for which there is some hope. However, the Sub-Committee may wish to explore the more radical option of complete closure. No doubt this would create severe political difficulties. But it would be little more expensive than partial closure, even in the short

CONFIDENTIAL

term; and it would offer substantial savings in the longer term. It is far from clear, on the evidence before the Sub-Committee, that there is any prospect of a profitable merchant shipbuilding industry in this country.

8. Points that the Sub-Committee may wish to explore are as follows.

(a) What is the financial test which will demonstrate that there is a 'viable core'? When is it supposed to break even, without Intervention Fund assistance or any other subsidy?

(b) Why must assistance of as much as £100 million over the next two years be directed towards the better BS yards? Mr Parkinson cites the recession and price competition from the Far East. But the latter will be a continuing problem, not just a problem for the next two years.

(c) Is there an option for BS which involves keeping fewer than 9,000 men in merchant shipbuilding?

9. It may well be argued against this that Ministers would need a good deal more evidence before they could contemplate so drastic a step as complete closure. If so, a possible approach would be to ask Mr Day to consider this as an option (ie not to assume that it is ruled out for political reasons) and to advise on the desirability of this and other courses as part of the exercise recommended at the start of paragraph 27 of E(NI)(83)15.

Implications for individual yards

10. We understand that any worthwhile rationalisation programme is likely to involve closing Scott Lithgow; Henry Robb (Leith); Ferguson/Aika (Clyde and Ayrshire); Smiths Dock (Teesside) and probably Swan Hunter (Tyneside). Closing any of these yards would be difficult: specially so in the case of Scott Lithgow and Swan Hunter. But you will probably want to avoid prolonged discussion of individual yards at this meeting. It is for Mr Day to advise the Government which ones should be closed: and it would defeat the point of trying to rationalise BS if Ministers seek now to make a special case for retaining particular yards.

European Community Implications

11. Under the Fifth Shipbuilding Directive, production aids for shipbuilding can only be paid with the prior approval of the European Commission. It will not be easy to obtain Commission approval to an effective doubling of the current rate of Intervention Fund subsidy; production aids are supposed to be 'degressive' under the Fifth Directive; the size of BS's losses and loss financing in 1982-83 will also influence the Commission's attitude. The Commission may however be prepared to accept an increase in the intensity of aid for a limited period if this is accompanied by significant rationalisation, like that which the Secretary of State proposes; they will probably look for yard closures and not just redundancies.

12. If the Sub-Committee should decide that total closure is an option that should be explored, this would presumably have a considerable effect on our tactics.

13. It might therefore be best to invite the Secretary of State for Trade and Industry and the Foreign and Commonwealth Secretary to arrange for officials to discuss the tactics and timing of an approach to the Commission in the light of the Sub-Committee's decisions on the substance.

Achieving the Government's Objectives.

14. It has proved consistently difficult to get BS to face up to its problems, produce realistic plans and stick to them. No doubt Mr Day's arrival will improve matters; but how does the Secretary of State intend to ensure that the Government's objectives are achieved? In particular:

→ (a) Will he make clear to Mr Day what order of run down the Government is prepared to accept? (Depending on the course of the Sub-Committee's discussion this could extend to total closure of merchant shipbuilding and perhaps other activities).

(b) When does he envisage reaching agreement with Mr Day about the latter's objectives as Chairman of BS? Will the objectives specify a timetable for BS to break even or make profits on merchant and offshore work?

(c) When is Mr Day to be asked to report back with his advice on contraction?

see  
m/s FCO to  
S/S DTI 13/7

flag c

Warships

15. The Sub-Committee is likely to welcome the Secretary of State's proposal to explore how the financial control of warshipbuilding might be separated from that of BS's other activities, so as to facilitate privatisation and to clarify the financial performance of the Corporation's divisions.

Ship-repair

16. Mr Parkinson says that he hopes to see substantial progress by BS in closing down or getting rid of ship-repair facilities by the end of 1983-84. Does he envisage that all of these activities can be got rid of by the end of the financial year, as the Sub-Committee intended when it last discussed BS?

Engine building and engineering

17. When does the Secretary of State intend to bring forward proposals to deal with the excess capacity in these activities?

External Financing Limit.

18. Mr Parkinson proposes that BS's EFL for this year should be raised from £159 million to £174 million (an increase of £16 million less a cut of £1 million as a contribution towards last week's measures). I understand that the Treasury are content with this proposal.

HANDLING

19. The Secretary of State for Trade and Industry will want to introduce his proposals. The Chancellor of the Exchequer or the Chief Secretary, Treasury will wish to comment generally on them, as may Mr Sparrow and the Chancellor of the Duchy of Lancaster. The Secretary of State for Scotland will wish to comment on the implications for Scotland of the proposals before E(NI); so may the Secretary of State for Northern Ireland and the Secretary of State for Defence on their implications respectively for Harland and Wolff and warshipbuilding. The Secretary of State for Foreign and Commonwealth Affairs (or his representative) will wish to discuss the European Community implications of the proposals. The Minister of State, Department of Trade and Industry (Mr Lamont) will be able to deal with any detailed questions which arise about the industry.

CONFIDENTIAL

CONCLUSIONS

20. You will want E(NI) to reach conclusions on the proposals summarised in paragraph 27 of E(NI)(83)15, ie:

- Need to  
concentrate  
better words.*
- 179 -*
- i. in respect of merchant shipbuilding:
    - a. whether BS should be told to prepare a plan for "controlled rundown", ie partial closure (preserving 9000 jobs) or whether other courses, such as total closure, should also be examined;
    - b. whether an approach should be made to the Commission immediately for approval of Intervention Fund assistance amounting to around £100 million over 1983-84 and 1984-85;
  - ii. whether the offshore division should be run down by the closure of Scott Lithgow in 1985;
  - iii. whether warshipbuilding should be privatised wherever possible (and the feasibility of separate financial arrangements for this activity explored as a step towards this);
  - iv. whether BS should divest themselves of their ship repair and engineering activities;
  - v. whether the future of engine building should be considered in the light of the future of merchant shipbuilding;
  - vi. whether BSs' EFL for 1983-84 should be raised to £175\* million;
  - vii. whether the future of BS should be considered again in the autumn on the basis of a new Corporate Plan by the new Chairman, taking account of i. to vi. above.

*PLG*  
P L GREGSON

13 July 1983