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21/12/84 C.P. Wainwright

PRIME MINISTER

CAMMELL LAIRD AND TYPE 22 FRIGATES

I have seen Michael Heseltine's minute to you of 18 December proposing to place one Type 22 frigate order with Swan Hunter and one with Cammell Laird.

2 I think we need to look at this proposal very carefully, in the light of the wider implications that will flow from our decision on these orders. I am sure that you will recall that we agreed in Cabinet in July (CC(84)27th meeting) that there should be a further round of tendering for the two Type 22 frigates, on the basis of a realistic assessment of the overheads of the yards involved. As I said at the time, Cammell Laird only "won" the two earlier rounds because they had assumed that overheads would be spread over other work - an assumption that had already proved to be wrong in July, since at that time their management accounts were forecasting a loss of over £7m on the price they were then quoting. Since that time their overheads have in fact come down because of the redundancies they have now put into effect, but unfortunately this has been insufficient to allow them to win other work. Even so, British Shipbuilders (BS) did allow them to assume that they would be allowed to spread their overheads over a large refit contract for MOD for the Balder London (which I understand MOD no longer intend to proceed with) and a large amount of unspecified work equivalent to a Type 2400 submarine and the third AOR vessel. Despite misgivings, BS also allowed them to assume a saving in overheads of £1.4m per annum from a priority based budgeting exercise.

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3 It is true that BS did not allow Cammell Laird to bid for both Type 22 frigates in the latest round of tenders, because they could not do both with their reduced labour force (1700) without recruiting 800 extra workers. This would obviously not be sensible when there is patent overcapacity in this sector. Both Swan Hunter and Vosper Thornycroft have already had to declare redundancies recently (2,100 and 790 respectively) and both yards will have to declare more if they are unsuccessful. That is, BS would have to fire 800 men in the North-East or on the south coast in order to re-employ 800 men on Merseyside, which I do not find an attractive or an economic proposition.

4 I cannot therefore accept in any way the suggestion that the current round of tendering has been fixed. The process which Cabinet asked to be set in hand has been completed. The straightforward solution would be to accept the result and place both orders with Swan Hunter forthwith, at a considerable saving (some £6m) to the Defence vote and avoiding even greater additional costs to British Shipbuilders; the latter I assume Michael would also wish to carry on his budget.

5 In addition to the arguments about which tenders are the cheapest - which are of course ultimately for Michael - there are other financial implications flowing from the placing of these orders which are of concern to me. Michael's proposal would add significantly to BS's costs through increased under-recovery of overheads and the likely reduction in privatisation proceeds. It would certainly directly depress the sale price of Swan Hunter, and - since the award of a Type 22 frigate to Cammell Laird would manifestly leave the overcapacity problem unresolved - would indirectly affect the sale price of all the yards making large surface ships. I am



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not yet in a position to quantify the effects, but they would be likely to exceed by several times the direct difference in tender prices. It would hardly be right that any such extra costs to BS should be borne by DTI.

6 Aside from the question of costs, there is also the effect of a decision to place an order with Cammell Laird on the workforces of Swan Hunter and Vosper Thornycroft against the outcome of the tender process. Not only would such a decision be quite unfair and a poor reward for the loyalty and continuing moderation of the entire workforces at both yards in the face of large scale redundancies, but in Swan Hunter's case it should be recognised that unemployment in Tyne and Wear is as high as it is on Merseyside.

7 I should, however, make it clear that I am not opposed to considering with Michael some other action in favour of Cammell Laird if colleagues feel it is necessary to do so, either because of the general situation on Merseyside or because of the efforts of the Back to Work Committee. But any such action would need to be less damaging to the other yards and their workforces than the placing of an order there for a Type 22 frigate.

8 It is possible, even without an order, that someone (possibly from the offshore industry) might buy Cammell Laird as a going concern, but this is far from certain. The chances of disposing of Cammell Laird as a going concern would certainly be improved if they had a workload to tide them over while a new owner finds new work. Perhaps the best way to do this would be for MOD to place with the yard an order for a refit on a non-competitive basis.

9 Such a solution should be considerably cheaper and less

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damaging to our broader plans for shipbuilding than the one proposed by Michael, and would offer a real prospect of a future for at least some of the workforce at Cammell Laird.

10 I hope that you and colleagues will agree that we should discuss the matter after the holiday.

11 I am sending copies of this minute to the members of the Cabinet and to Sir Robert Armstrong.

momentarily
PP

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21 December 1984

*Seen and approved by the
Secretary of State, and
signed in his enforced absence*

Department of Trade and Industry

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