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PRIME MINISTER

British Steel Corporation Future Strategy

BACKGROUND

You are holding a meeting with the Ministers most closely concerned at 10.00 am on Monday 6 December to discuss the future strategy of the British Steel Corporation (BSC). In preparation for that meeting the Secretary of State for Industry has circulated, with his minute of 2 December, a paper describing the current outlook and making proposals for action.

2. Mainly because of a decline in the world market for steel and a reduction in BSC's share of the market, BSC's financial prospects have worsened severely. Losses are running at about £7 million a week; the expected total loss in 1982-83 is about £200 million before interest (£200 million worse than plan); if no offsetting action is taken the forecast loss for 1983-84 is £380 million (over £400 million worse than plan). A number of measures to reduce costs are in hand; but the BSC consider that they cannot achieve lasting profitability without closing one of their five integrated steel works. In particular, they think they will need to close one of the three hot strip mills (at Ravenscraig, Port Talbot, and Llanwern); and that if closure takes place quickly it should be at Ravenscraig.

3. The Secretary of State for Industry suggests that the Government must maintain its objective that the BSC should be profitable without Government subsidy and should eventually be restored to the private sector. Unless the Government expects a large, early and substantial upturn in the demand for steel (and there is no reason to do so), this entails closure of a major integrated works. He considers four options:

- (i) close Ravenscraig as soon as possible;
- (ii) decide to close a strip mill, but defer the choice of works for two or three years;





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- (iii) an early partial closure in the Ravenscraig complex, with the implication that Ravenscraig has no long term future;
- (iv) deferring the question of closure altogether.

He recommends option ii.

4. The Secretary of State also advocates a decision in principle in favour of BSC's proposals for modernising the hot strip mill at Port Talbot, costing some £175 million. He recognises that, among other things, this will create difficulties with the European Commission (who would not approve substantial new investment in current circumstances of excess capacity unless accompanied by a reduction in capacity elsewhere). But he suggests that they could be solved by a 'contract to limit output'

5. The Secretary of State also makes proposals on presentation, and suggests that he should circulate the draft of a Parliamentary statement reflecting the Government's decisions.

#### MAIN ISSUES

6. The main issues for the meeting are as follows.
- (i) Is the closure of a major integrated steel works necessary?
  - (ii) If so, which should it be?
  - (iii) Should the proposed investment at Port Talbot be approved?
  - (iv) How should relations with the Commission be handled?
  - (v) How should the Government decisions be announced?

#### Is closure necessary?

7. To decide not to close any of the large integrated steel works would be tantamount to accepting that the BSC will not be profitable for the foreseeable future. This would be a complete reversal of existing policy. A closure therefore seems inescapable sooner or later. It is relevant that the short-term forecasts in the paper seem more likely to be optimistic than pessimistic.





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They assume, for example, that BSC will secure 50 per cent of the UK market (compared with their present share of 48 per cent) and exports at the same level as in the current year, despite the weakening of the world market and the restrictions on imports imposed by the USA.

Which works should be closed?

8. It seems inescapable that if closure is to be immediate it should take place at Ravenscraig: the BSC assessment in Annex 2 to the paper points unambiguously in that direction. But the Secretary of State argues that closure should be deferred for two or three years. The choice of works would then also be deferred, since it is possible that performance at Ravenscraig would improve enough to make it preferable to close Llanwern. Unemployment there, though high, is lower than at Ravenscraig; and existing consumer preference for Llanwern is expected to decline because Llanwern cannot, without substantial new investment, produce continuously cast feed stock. The decision therefore turns on timing.

9. The Secretary of State for Industry advances some powerful arguments for delay.

(i) It would strengthen our hand in demanding reductions in steel-making capacity from our European partners.

(ii) Immediate closure of Ravenscraig would produce very high unemployment in the area - about 30 per cent male unemployment, after allowing for consequential effects of closure.

(iii) It would avoid some (probably fairly small) loss of markets to imported steel.

(iv) It would at least postpone the need for £100 million investment in continuous casting facilities in South Wales: customer preference is for continuously cast feedstock, which Ravenscraig produces but Llanwern does not.

But there are also arguments on the other side, which you will want the meeting to explore.





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(v) Delay may jeopardise the necessary improvement in BSC's finances.

(vi) It is also likely seriously to complicate negotiations with the Commission.

10. Most importantly, it must be doubtful whether it would be possible to prevent it from becoming known that the Government and BSC expected a major closure in two or three years time. Apart from the usual risk of leaks, the Commission would be bound to press for an indication of our intention to reduce capacity, especially if they were being asked to approve the proposed new investment at Port Talbot. Other European countries would ask why the UK was being allowed to install substantial new capacity without making reductions elsewhere. If it were to become known that a major closure was in prospect, but no decision had been made between Ravenscraig and Llanwern, the Government would face very heavy pressure from both areas.

*it would cast a blight upon both areas?*

*MCS*

Proposed investment at Port Talbot

11. There is a strong case for further investment at Port Talbot. This is already the BSC's lowest-cost strip steel producer; but it will need to be kept up to date if it is to stay competitive on international markets. However, we understand that a fully worked out case has not yet been presented by the BSC; and there may well be questions about, for example, the exact timing of investment which need consideration. You may feel that the BSC should be invited to make out a proper case in the context of their corporate plan.

Relations with the European Commission

12. It is possible that there may be more difficulty with the Commission than the Secretary of State for Industry allows in paragraph 13 of his paper. It may be that they will insist on a public statement of intention to close a strip mill, not only as a condition for approving new investment at Port Talbot but also for approving further financial support. It cannot be taken for granted that the proposed 'contract' to limit output will be sufficient. No doubt it will be necessary to start confidential exploratory talks with the Commission as quickly as possible.





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### Announcements

13. The Secretary of State for Industry outlines a possible Parliamentary statement in paragraph 21 of his paper. It reflects the arguments he puts forward about the substance of the decisions, and has the same strengths and weaknesses. As he points out, it risks creating political problems at both Ravenscraig and Llanwern. It is also not easy to see how it can avoid either:

(i) implying that the financial situation of the BSC is not particularly serious (an implication that would be strengthened if and when an announcement is made of further investment at Port Talbot); or

(ii) admitting that the situation is serious, but implying that the Government and the BSC are deferring necessary corrective action because the political consequences are unpalatable.

### Other options

14. If other Ministers are doubtful whether the Secretary of State for Industry's option (ii) will work, because of the uncertainty which may be cast over both Ravenscraig and Llanwern, and are nevertheless reluctant to face the immediate closure of Ravenscraig, they may wish to look more carefully at the two remaining options - either the partial closure of Ravenscraig (option (iii)), or deferring a closure decision altogether (option (iv)). In either case it might be necessary to defer also the Port Talbot modernisation, but it could be argued that the case for going ahead with that substantial new investment in the near future has not yet been fully made out. Option (iii) would have the advantage that it would save some money (£15 million a year) and would enable the redundancies at Ravenscraig to be spread out over a longer period. Option (iv) is the least desirable option on economic and commercial grounds, but some Ministers may see political and social arguments in favour of it. They may point out that even under the Secretary of State for Industry's preferred option (ii), closure is to be deferred. Why therefore should the Government be forced into a decision now that one of the strip mills will definitely be closed?





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HANDLING

15. You will wish to ask the Secretary of State for Industry to introduce his paper. All the other Ministers present have a clear departmental interest and will no doubt want to contribute. Whatever the meeting may decide, the presentation of the decisions seems likely to be difficult; and you will wish to ensure that the meeting devotes sufficient attention to this aspect.

CONCLUSIONS

16. You will wish the meeting to reach conclusions on the following:

a. which of the following options should be adopted:

- (i) immediate closure of Ravenscraig;
- (ii) a decision to close one strip mill, with the choice deferred for 2 or 3 years;
- (iii) early partial closure of Ravenscraig;
- (iv) deferring a decision on closure altogether.

b. Should the proposed investment at Port Talbot be approved in principle?

c. How should relations with the Commission be handled?

d. How should the Government's decisions be announced?

17. Depending on the decisions reached, you will no doubt wish to invite the Secretary of State for Industry to circulate the draft of any statement. It is highly desirable that when he does so he should allow colleagues adequate time to consider the text: the presentation is almost certain to be very difficult.

*PLG*

P L GREGSON

3 December 1982