



10 DOWNING STREET

PRIME MINISTER

I attach a brief for your meeting with Mr. Ridley. You may also wish to note David Wolfson's comments, in the course of his note at Flag A, about the possibility of Walter Goldsmith heading the new NHS management team.

DAB

DAVID BARCLAY

17 November 1983

FILE 84
SUBJECT: Aeromarine: future of
British Airways
5/82

MEETING WITH SECRETARY OF STATE FOR TRANSPORT

Mr. Ridley is likely to raise the following topics at his meeting with you.

1. British Airways/British Caledonian
See David Wolfson's note about this, attached at Flag A and Policy Unit advice at Flag B.
2. British Airways Privatisation
Mr. Ridley is considering the possibility of proceeding without legislation. It might be possible to apply to the Companies Court for a write down of capital. This would mean that the timetable could be speeded up, but there is a significant risk of accusations of privatisation by the back door.
3. National Bus Company Privatisation
Mr. Ridley is inclined to go slow. There is no prospect of legislation this session so he would prefer to take time to get the competition framework and the subsidy regime right.
4. London Transport
Mr. Ridley is worried about concessionary fares. The Boroughs are supposed to be taking over responsibility when the GLC is abolished. They are using this as a lever to oppose abolition, and Mr. Ridley is some way from a satisfactory solution.

/ 5. Non-rail transport

5. Non-rail Transport Subsidies

The Secretary of State believes that transport subsidies other than rail subsidies (which he regards as inevitable) provide at best indeterminate value for money. He may propose a measure of transfer of resources from revenue subsidies to highway construction.

6. Ministerial Responsibilities

Finally, Mr. Ridley may wish to raise with you the possibility of some reinforcement of his Ministerial team at the Department of Transport.

DAVID BARCLAY

17 November, 1983



10 DOWNING STREET

Prime Minister.

Nov. 15, 1983.

A
SUBJECT Files on
Aerospac: Future of
B Airways

1. You are seeing Nick Ridley and will no doubt discuss British Caledonian's offer for British Airways routes.

The Policy Unit have advised you to ignore Adam Thompson's bid. Ivan Fallon would advise you differently. I draw to your attention that there are, in my opinion, two sides to the case. A Privatised British Airways, with over 80% of the market, making £150 Million per annum, would be able to destroy British Caledonian whenever it chose. The threat implied by a near-monopolist would be enough to inhibit competition.

There is a real dilemma: speed of privatisation, and simplicity, may speak in favour of leaving British Airways as it is, but the creation of a properly competitive market for British Scheduled passengers favors a partial break-up sale before privatisation.

2. I feel sure that we are going to face continuing attack on the Health Service over the next two years, during which time hopefully better management will be introduced to help the service provide more for less. While Walter Goldsmith has all the talents to head the management team, his political vibrations would be of the "axeman" variety. On reflection, I doubt that he would get a real chance to do the job. The fears of privatisation of the NHS would run riot, and a less publicly right wing choice seems more likely to succeed.

DW.

David Wolfson.

Not such a King-sized BA

FOR the past two years the aviation world, the Government and a large chunk of the public has watched Lord King's progress through British Airways with considerable astonishment.

There have been redundancies, massive losses (£540 million in a single year when everything including the kitchen sink was written down or written off), management changes, dissent and jubilation from opponents and supporters—and towards the end of the day the growing belief that King can actually achieve what he set out to do which is take the airline out of the State sector and privatise it.

Watching even more closely than the rest of us were Sir Adam Thomson and his men at the independent, fully-privatised British Caledonian, who have viewed it all with mixed feelings. Competing with an overblown inefficient, uncaring and unprofitable State-owned airline is one thing. Flying against a slim, motivated, private—and most important of all—decently financed airline, which is what BA could become by this time next year, is another.

So Sir Adam and his managing director Alastair Pugh concocted a plan of their own, one which Lord King does not like at all, but which the

Government, in the guise of new Transport Secretary Nicholas Ridley (for starters) will have to take seriously, even if it does potentially endanger the BA privatisation timetable.

The British Caledonian scheme is an ingenious and intellectually attractive one.

British Airways at present is seven times the size of Caledonian, and if nothing is done to change that on privatisation, four-fifths of Britain's scheduled air transport business will be controlled by one operator.

If BA had its debt wiped off and came to the stock market with a cleaned up balance sheet, which is about the only way it could attract outside investors, then the competition would become more unequal still.

The imbalance between the two airlines is paralleled by the imbalance between London's two airports, Heathrow and Gatwick. Again Heathrow is seven times larger on scheduled services. BCal represents the heart of Gatwick's scheduled business.

Operating out of Gatwick puts it at quite a disadvantage—and if the more formidable King-sized BA moved into the private sector, BCal might even move to Heathrow with all the implications that would have for both airports.

Such is the scene, viewed from Caledonian House, at Gatwick. So what to do about it?

COMMENT by Ivan Fallon

If BA is to be sold, BCal wants to buy at least a part of it. It has put itself first in the queue, before the City institutions, private investors or even BA's management.

It has picked out a series of routes which it reckons would boost both its own operations and Gatwick Airport, and offered £200 million for the assets that go with them.

These routes are still on the secret list, but are listed in BCal's blue book—and apparently include routes to the Caribbean, the Middle East, and Japan. BCal insist they are by no means BA's most profitable routes, but obviously they are not loss-makers either.

But the independent airline and Sir Adam Thomson have gone a stage further. They also suggest that BA be relieved of regional operations as well. BCal itself does not want them. But it suggests that operations based on the "mini-hubs" of Glasgow and Manchester, and possibly even the German internal routes, should be sold for cash to other specialist independents who could create strong locally-based concerns and run the routes more effectively than BA.

Now the effect of all this would be considerable. BCal itself



would increase in size by perhaps two-thirds—a quantum leap which otherwise would take it 10 to 15 years of hard slog. Its share of scheduled services would grow from 17 to 29 per cent, while other independents such as British Midland and Dan-Air would rise from 2 per cent to 5 per cent.

And British Airways? Instead of having four-fifths of British Scheduled passengers, it would drop to a healthy enough two-thirds. At that level it would still be the giant, but no longer quite so dominant. And if he could get his extra routes, Sir Adam and his friends would no longer kick up a fuss about write-offs of BA debt and cleaned up balance sheets.

In the past 10 years 14 independent British airlines have gone out of business, including of course Laker, Invicta, Skyways, Chamel, IAS and so on. It is difficult enough just to survive. To make headway in an industry dominated by state concerns is exceptionally difficult, which makes BCal's achievement all the more laudable.

What then is the argument against Sir Adam's plan? The sale of £200 million of assets would make BA a smaller airline, and, therefore, more easy to sell—and of course, there would be £200 million of cash up front before the operation got under way. But whatever argument Sir

Adam presents, the plan would tear a hole in BA's profitable operations, result in major redundancy payments all over again (BCal would not necessarily take all the people that went with its routes) and set back the privatisation timetable.

King himself might get so disillusioned that he would seek other pastures, and without him the privatisation momentum would run down, and so too would the drive for efficiency.

But maybe there is room for a delicate compromise. It does not have to be £200 million of assets—even a £100 million shift from BA to BCal, and of routes from Heathrow to Gatwick, would make a great deal of difference.

BCal is willing and able to offer the Government hard cash for assets independently valued in what is a genuine attempt to introduce greater long-term competition into the British airline business.

SUBJECT Files on:
Aeroplane: future of
B. Airways

MR. TURNBULL

MEETING WITH THE SECRETARY OF STATE FOR TRANSPORT

The Prime Minister has agreed to see the Secretary of State for Transport next week.

I understand from Dinah Nichols that he is likely to raise three topics:-

- (i) British Airways Privatisation - He is considering the possibility of proceeding with BA privatisation without legislation. Apparently it would be possible to apply to the Companies' Court for a write down of capital. This would mean that the timetable could be considerably speeded up, so that flotation could proceed at a decent interval after British Telecom, or at the time currently scheduled for British Telecom if this slips. On the other hand, there must be a considerable risk that such a procedure would be criticised as unfair circumvention of Parliament.
- (ii) London Transport - Mr. Ridley will wish to discuss particularly concessionary fares. As you know, the current proposal is that when the GLC is abolished the London Boroughs should take over full responsibility for concessionary fares. This is a sensitive political issue, which the London local authorities are exploiting in their opposition to local government reform, and Mr. Ridley is apparently by no means confident that a satisfactory solution is at hand.

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(iii) Ministerial Responsibilities - I understand that Mr. Ridley may also ask the Prime Minister for some reinforcement of his Ministerial team at the Department of Transport, to reflect his enlarged responsibilities...

sub

DAVID BARCLAY

11 November 1983

cf For meeting with S/S for
Transport on Thursday please.
SUBJECT: Aerospace: future of
B Airways
c Mr Alison
DMS
15/11

MR. TURNBULL

Meeting with the S/S for Transport

Since I dictated the attached note to you about the Prime Minister's meeting next week with Mr. Ridley, Dinah Nichols has suggested two further topics.

They are:

- i. NBC privatisation - Mr. Ridley is inclined to go slow on this. There is no prospect of legislation in the current session, so he would prefer to take his time in getting the competition and subsidy framework right.
- ii. Non-rail transport subsidies - Mr. Ridley may express a general view that transport subsidies (other than rail subsidies, which he regards as inevitable) provide indeterminate value for money. He may say that he is aiming to transfer resources from revenue subsidies to highway construction.

DMS

11 November 1983