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CABINET

THE 'SECOND FORCE' AIRLINE

Memorandum by the President of the Board of Trade

1. We are committed to encouraging the creation of a 'second force' independent airline. The only way in which such an airline can be created in the foreseeable future is through the purchase of British United Airways (BUA) by Caledonian. For this purpose it will be necessary to secure some transfer of routes from the two Air Corporations.
2. Caledonian are confident that they can finance the purchase of BUA (which involves a total commitment of about £32 million) provided they can satisfy their existing and potential shareholders that routes will be transferred to the new airline on a scale sufficient to yield an additional profit before tax of about £800,000 in 1971, or a rather higher figure if the routes are not transferred until 1972 or later. This would mean the transfer of routes yielding a revenue of about £5-£6 million in 1971, compared with British Overseas Airways Corporation's (BOAC's) total current revenue of £200 million. BOAC's profits are likely to be affected to a greater extent proportionately as total profitability looks like declining over the next few years.
3. The Chairmen of the Air Corporations have made it clear that their Boards will not agree voluntarily to give up routes. It follows that if the Government wants to go ahead it will have to use its statutory powers. Once these powers are invoked there is no reason to believe the Corporations will not co-operate.
4. The Law Officers have confirmed that I have powers the exercise of which would result in a transfer of routes from BOAC (and perhaps, to a lesser extent, from British European Airways) to Caledonian. There is no precedent for the use of these powers for this purpose and we may be criticised for bypassing the ordinary Air Transport Licensing Board licensing machinery. The ordinary control over Nationalised Industry investment will enable me to stop BOAC acquiring BUA.

5. The situation has been deteriorating rapidly recently in two respects following leaks to the Press. BUA has been losing traffic since people are unwilling to book on an airline which might cease operations soon. The morale of BUA employees is poor and there are signs that it may worsen rapidly. Secondly, in pursuit of a claim for complete parity of pay and conditions with the Air Corporations, the unions have threatened to go on strike from 3 August.

6. After an exceptionally profitable year in 1969 BUA's profits have sharply declined and these could become substantial losses if current union demands for parity of pay and conditions with BOAC were conceded. In this situation Sir Nicholas Cayzer might possibly decide to put BUA into liquidation or to concede complete parity in order to avoid a strike. If BUA were to be liquidated there would be no certainty that Caledonian would be able to pick up the routes that would enable them to operate as a 'second force' airline, since all airlines would be able to bid and the ordinary long drawn out licensing procedures would have to be used. Moreover, in these circumstances, it would be much more difficult to justify the transfer of some BOAC routes to Caledonian. In the resulting confusion and uncertainty Caledonian's present financial backers would almost certainly lose interest.

7. If on the other hand BUA continued operations but conceded complete parity the new airline resulting from a Caledonian purchase of BUA would have greater difficulty in attaining the profitability it needs to attract continuing financial support. This concession might make the purchase of BUA impossible for any airline except BOAC. Caledonian would be prepared to pay comparable rates for comparable work, which in effect means parity in basic rates but intend to negotiate with the unions to secure comparable productivity agreements (and possibly some staging of their increased commitments). This is a different matter from proceeding to immediate parity in pay irrespective of productivity.

8. In the face of these risks I felt that I ought to make an immediate statement on the lines of the attached draft. When the Ministerial Committee on Economic Policy considered this statement on 27 July there was general agreement that the Government should pursue vigorously its policy of fostering the 'second force' in spite of strong opposition from the trade unions and the Air Corporations. It was, however, essential to get both the timing and the context of the statement right. The statement, if issued too early, might prejudice the chances of securing an early agreement to end the dock strike. It would also be a great pity if the 'second force' airline came to be publicly suspect as one run on cheap labour, or if its launching coincided with strikes in BUA and in the Air Corporations. If at all possible the BUA pay claim should be publicly seen to be a quite different issue from the 'second force'.

9. As matters are developing, however, I consider that we should not delay our statement any longer, because of the risk that precipitate action by Sir Nicholas Cayzer or by the BUA employees might jeopardise the whole concept of a 'second force' airline. I understand that Caledonian are prepared to move quickly to comparable pay for comparable work and there is evidence to suggest that, faced with a Government decision, the unions would negotiate with Caledonian as the prospective employer and would not force an immediate strike on 3 August. There have been suggestions that Mr Clive Jenkins might call out Air Corporation staff to prevent a transfer of routes. I do not think we can concede to such pressures.

10. It is also for consideration whether I should be authorised to say that the Government will not, in any event, be prepared to approve a purchase of BUA by BOAC. Sir Nicholas Cayzer has continued to hope that, in the last analysis, the Government would approve such a purchase and for this reason he has not been as forthcoming as he might have been in his dealings with Caledonian. A statement on these lines would force both him and the unions to be more realistic in their dealings with Caledonian. On the other hand, the hope of an ultimate sale to BOAC may be one of the factors which will deter him from going into liquidation. I think we may have to make such a statement, but I would prefer to hold it until it is shown to be essential.

CONCLUSION

11. I therefore seek the agreement of my colleagues to the issue of the attached statement without more delay. It would have the effect of enabling Caledonian at once to start negotiation with BUA and to start discussing with the unions as the prospective 'second force' airline the standards of pay and productivity which should apply. I should like further to have authority to tell Sir Nicholas Cayzer, should this prove necessary, that the Government do not intend to permit BOAC to purchase BUA if the deal with Caledonian falls through. We must be clear, however, that this could increase the possibility that BUA might be put into liquidation, with the consequences outlined above. We may have to take this risk.

M A C N

Board of Trade SW1

28 July 1970

CIVIL AVIATION

A SECOND FORCE INDEPENDENT AIRLINE

The Government wish the private sector of the civil aviation industry to be given the opportunity to form by amalgamation a "second force" airline that would fill the role of second flag carrier on major international routes as well as sustaining extensive charter services. Such an airline, combining the resources and skills of British United and Caledonian, could provide a powerful additional source of airline management and innovation; its existence would permit the licensing of a second British carrier on those international routes such as the North Atlantic where this should increase the traffic carried by British airlines; and it could serve those domestic routes where it was desirable to offer the public a choice of airlines.

2. The Government accept that such a new airline, if it can measure up to its task, should be given preference over other operators in the licensing of new scheduled routes that would contribute to a viable route network, in the licensing of a second carrier on existing scheduled routes or in any sector of the market (such as long-haul inclusive tour charters) where there may for a time be room for only a limited number of operators. Where the new airline is licensed to serve a domestic route jointly with another operator, they accept the need progressively to relax any restrictions on the frequency of services. They also accept that some exceptional transfer of routes from the public sector - and possibly some rationalisation, including an exchange of routes - will be necessary in the initial stages, though not as a continuing process, if the new airline is to have a sufficient basis at the outset.

3. BOAC's total revenue is about £200m. Forecasts of inter-continental traffic point to an expansion of about 14% a year up to 1975. Against the background of such growth a modest transfer of routes from BOAC to the new airline, representing something of the order of 2½% or 3% of their current annual revenue, would have small impact on BOAC's continuing expansion. Both revenue and employment will continue to increase. The return on the public investment need not be unduly impaired so long as the routes transferred from either Corporation did not significantly affect the overall efficiency of their operations.

4. The Air Corporations must remain our principal flag carriers bearing as in the past the main weight of this country's civil aviation effort. The routes to be transferred must therefore be so chosen as to combine with the overall national interest the maximum benefit to the viability of the new airline with the least impact on the Air Corporations.

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5. The civil aviation industry has been subject to much uncertainty since 1967 and it is desirable that matters should be brought to a conclusion without further delay. The Government are considering legislation based on the recommendations of the Edwards Committee for changes in the regulatory machinery; they accept, in principle, the establishment of a licensing authority whose decisions will be governed by a formal statement of policy which will reflect, among other things, the considerations set out in this White Paper. However, the Government consider it important that the new airline should be formed as quickly as possible and should have new routes to serve by the summer of 1971. They would prefer the arrangements for the transfer of routes to be made through normal licensing procedures after discussion with the airlines concerned. They accept, however, that the Air Corporations will not willingly give up even a small sector of their routes. If necessary, therefore, pending the new legislation, they will be prepared to use their powers under Section 3(5) of the Air Corporations Act 1967 and under Section 1(3) of the Civil Aviation (Licensing) Act 1960, to ensure that the intended outcome is not unduly delayed.

6. It is in the best interests of the industry and of the country that a stable and viable solution should be found quickly. In particular it is in the interests of those who work in BUA and in Caledonian that the new flag carrier should have the strength and opportunities that will enable it to move quickly towards terms and conditions of employment comparable with those offered by the Air Corporations for comparable work.

