University of Strathclyde

The Fraser of Allander Institute

Quarterly Economic Commentary

FRASER of ALLANDER INSTITUTE

The Fraser of Allander Institute for Research on the Scottish Economy was established in the University of Strathclyde on 1 January 1975, as the result of a generous donation from the Hugh Fraser Foundation. Its principal function is to carry out research on the Scottish economy and its research programme includes the analysis of short term movements in economic activity. The results of this work, carried out in conjunction with the Department of Economics, are published in the Institute's Quarterly Economic Commentary. The Institute also publishes a series of Research Monographs and a series of Discussion Papers to provide an outlet for original research on medium term and long term aspects of the Scottish economy.

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Notes to contributors

The editor welcomes contributions to the Briefing Paper, Feature Article and Economic Perspective sections. Material submitted should be of interest to a predominantly Scottish readership and written in a style intelligible to a non-specialist audience. Footnotes and references should conform to recent issues of the Commentary. Contributions should be typed and two copies submitted to the Editor.

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QUARTERLY ECONOMIC COMMENTARY

Opinions expressed in signed contributions are those of the authors and not necessarily those of the Fraser Institute.

Outlook and Appraisal

The most recent **Scottish Business Survey** reports a continuing rise in optimism among Scottish retailers and some cautious improvement for manufacturers. In line with the recent resurgence in consumers expenditure at the national level, Scottish retailers are enjoying considerable increases in sales volumes. The more cautious view among manufacturers probably reflects concern over the apparent reduction in the relative importance of export markets as a source of new orders and sales. Sterling's appreciation, to a level forecast late last year by the Fraser of Allander Institute, place s Scottish manufacturers under greater competitive pressure abroad (and domestically) and adds an element of fragility to the recovery of output. Scottish wholesalers and, particularly, construction companies are less optimistic about business conditions. In the latter case, the major cause continues to be the decline in orders from the public sector.

The **Survey** provides little indication that employment is likely to expand. Further full-time job losses are forecast in construction, wholesaling and distribution, although in the latter two sectors increases in part-time employment will occur. Encouragingly, after recent signs of an end to labour-shedding, there is evidence that manufacturers may hire some, albeit limited, additional labour in the near future.

The single major development has been, however, the announcement from the British Steel Corporation in August that the Gartcosh rolling mill will be closed at the end of March next year and that the Ravenscraig plant, like other UK plants, is not to receive new investment in coke ovens. Despite extensive lobbying by a wide range of Scottish organisations for complete replacement of an existing battery of coke ovens to secure a longer-term future for the Ravenscraig plant, it became increasingly apparent over the summer that the option of not replacing the coke ovens was the likely outcome. These decisions probably signal the end of the Scottish steel-making industry by the end of the decade.

Closure of the Gartcosh mill does not in itself lead automatically to the closure of the main Ravenscraig plant. Gartcosh rolls and finishes around one-third of Ravenscraig's production of coils of wide strip steel for use in the manufacture of vehicles and domestic appliances. After 1986 those coils will be transferred to other BSC mills for finishing as happens at present with the bulk of Ravenscraig's output. It would be misleading, however, to suggest anything other than that the Gartcosh closure makes Revenscraig's future extremely precarious. The loss of an adjacent customer and the lower output levels attendant on the likelihood of increases in production at Llanwern and Port Talbot for the vehicle and domestic appliance industries will raise Ravenscraig's unit production costs, a disadvantage that will certainly be held against Ravenscraig in the next comprehensive review of BSC's operations in 1988. Closure of capacity in Scotland and concentration of production of strip steel in the Welsh plants has been the thrust of BSC's policy throughout the 1980's.

BSC is charged by the Government with responsibility for achieving commercial viability and with preparing the industry for privatisation and has argued repeatedly that these objectives cannot be met, given likely demand for steel, without closure of one of the three UK strip mills. Demand prospects are poor for UK and other European producers in the USA where protectionist measures are being increasingly applied and in Third World markets where local capacity has expanded substantially and where it is difficult to compete with, for example, the Japanese. Within Europe the Davignon Plan for restructuring the industry has involved capacity reductions over the past five years.

Last year the House of Commons Select Committee on Trade and Industry defended Ravenscraig on the grounds that BSC's view of European market demand is unduly pessimistic. With productivity in UK plants above the European average it was felt that BSC might make significant gains in free European markets after the intended removal of the Davignon controls at the end of 1985. However, the Davignon strategy has not achieved its desired aims and some forms of control will remain.

Unlike other European countries, particularly Italy and France, the UK has met its targets for capacity reductions and those targets have not to date required the closure of a strip mill. Negotiations are currently in progress on the restructuring of the European industry to 1990. Although the exact outcome of these negotiations is unclear as yet. the EEC has already announced that by 1990 capacity reductions similar in scale to those of the past five years will be required to balance supply of and demand for European steel. In the near future, therefore, BSC is likely to be seeking further capacity reductions in line with EEC restructuring plans. The EEC has also in the recent past been of the view, perhaps inspired by BSC's own position, that one of the three UK strip mills should be closed.

Ravenscraig has consistently been identified as the likely candidate for closure as a consequence of its locational disadvantage. With the decline of metal-using industries in Scotland, Ravenscraig is more remote from the main UK markets in the Midlands and South East of England than the Welsh plants. It is also located inland from the deep-water terminal at Hunterston and, unlike the Welsh plants, its rolling mill has been some distance from the main complex, a difficulty now much compounded by the imminent closure of Gartcosh.

The principal advantage Ravenscraig held over its main rival for survival, Llanwern, was the ability to produce finished steel of a high and consistent quality as a consequence of its continuous casting facilities. With BSC's purchase and planned closure of the privately-owned company Alphasteel. that advantage has been removed. Alphasteel's continuous casting facilities are to be refurbished and installed at Llanwern

The successful defence of Ravenscraig in late 1982 was based largely on social and regional considerations. Closure of the Ravenscraig plant will undoubtedly impose substantial social costs on the Scottish economy. The most severe impact will be felt in the Motherwell area where the loss of over 3,000 jobs will exacerbate the already high level of unemployment. and the associated fall in income will generate secondary job losses in, for example, local retailing. Suppliers of goods and services such as British Gas, British Rail, SSEB, the Clyde Port Authority, British Oxygen. road-hauliers and catering, cleaning, crane-hire and security companies, will also lose an important customer. There is little prospect of these social costs being offset by new investment and certainly not on the scale that would be necessary to offset the effects on employment of Ravenscraig's closure.

In 1982 the social and regional arguments attracted all-party political support within Scotland and still do. Recently much Government goodwill was generated by the Ravenscraig's workers' refusal to support the NUM during the miners' dispute. It is clear, however, from Norman Tebbit's comments on the new BSC strategy that market and privatisation considerations will prevail. Social and regional factors now appear not to enter the calculus. The new strategy is also convenient both politically and commercially. It satisfies the Government's wish to present a political commitment to the main complex during the lifetime of this Parliament and BSC's need for Ravenscraig's output while the Redcar blast furnace is rebuilt next year and until refurbishment projects are completed at Llanwern and Port Talbot.

By 1988 Ravencraig's long-standing locational disadvantage will be compounded by a dire need for new investment in not only coke ovens but also by then a blast furnace. The commercial, privatisation and EEC restructuring objectives will then almost certainly dictate Ravenscraig's closure with considerable attendant costs to the Scottish economy.

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