

PRIME MINISTER

This is a letter from Arthur Knight saying that the NEB have now concluded that INMOS should go to South Wales! The reason for this appears to be that, because of rising costs, INMOS will need the extra regional grants which would be available if they go there.

Of course, it is for decision whether it would be right to allow them this extra money. Sir Keith will be coming back to E Committee next week, and if you agree, I will simply acknowledge.

*Agreed  
not.*

*TL*

22 July, 1980.

# National Enterprise Board

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COMMERCIAL IN CONFIDENCE

AWK/B/sar

18th July, 1980.

The Rt Hon Sir Keith Joseph, MP, Bt,  
Secretary of State for Industry,  
Department of Industry,  
Ashdown House,  
123 Victoria Street,  
London. SW1E 6RB

*Dear Keith,*

As you know I decided to conduct a review of the INMOS project because six months had elapsed since we decided, on the basis of INMOS' 1979 corporate plan, to approve a second £25 million in NEB funding for the project. The review which has taken about four weeks, was conducted by a team under Mr G R Jefferson, Chairman and Chief Executive of British Aerospace Dynamics Group and an NEB Board member. In laying down detailed terms of reference for the technical and commercial evaluation of the project, Mr Jefferson drew on advice from Sir Robert Clayton, Technical Director of GEC Limited, also an NEB Board member.

The review was split into four sections:

- (a) An examination of INMOS' management structure and of the company's progress to date in establishing a capability in the following areas: design, production, marketing, and cost and quality control.
- (b) A detailed technical evaluation of those INMOS products already at the prototype or design stage. This evaluation was carried out by a team from the British Aerospace Dynamics Group who had themselves established a MOS chip-making facility at BAe in Stevenage.
- (c) Two studies, by independent consultants (DATAQUEST and MOSAID, who are both leading North American consultancy firms) of the world MOS semiconductor market and of INMOS' position in that market, with particular reference to the fact that future supply might exceed demand (or vice versa).
- (d) An examination of INMOS' financial plans including sensitivity analyses based on relatively pessimistic assumptions on price, market growth, and the speed with which the company would gain market share.

The review team concluded that INMOS' management structure is generally sound and that the company is particularly strong in design and production. The technical evaluation established that INMOS' first products (the 16K static RAM and the 64K dynamic RAM which have already been announced) are at the leading edge of MOS technology and both products are on target. The independent studies of the world market for MOS products suggested that, because INMOS' major competitors have made very slow progress, the INMOS 16K static RAM could well be amongst the first on the market and, provided the design is successful, the INMOS 64K dynamic RAM should also be well within the window of opportunity. INMOS has assembled a very talented team at a time when design skills appear to be at a premium. For the future, the company has a well-developed series of new product plans encompassing inter alia an extension of its current and CMOS technology.

The review team's examination of INMOS' financial situation shows clearly that the high rates of UK inflation in the past year have reduced the purchasing power of the £50 million equity envisaged in the company's financing plans. This, and in particular the increase in UK building costs, have greatly enhanced the case for siting the company's first UK production unit (UK1) in an Assisted Area, where the company can take advantage of grants and other financial assistance which might be available.

At the same time the review team found that the technical progress made by the company in the last 6-9 months has greatly increased INMOS' confidence in its ability to manufacture its products successfully in the UK. As a result, although co-location of UK1 and the UK technology centre was a desirable objective, the company is now satisfied that it would be possible for UK1 and the technology centre to operate separately, provided the geographical separation is reasonable.

The NEB Board considered the findings of the review team at its meeting on 18 July, 1980. It agreed that in the light of progress made by the company to date, it would be unwise to call a halt to the project at this stage.

The Board considered whether, if restricted to the initial £25 million, INMOS could be developed into a profitable company, thus enabling the NEB to dispose of its shareholdings at a profit. The Board noted that in this eventuality the company would probably close down its UK operations and concentrate all its resources on the Colorado Springs factory. The sensitivity analyses done by the review team indicate that, on the most pessimistic assumptions, the risks attached to this option are excessively high, though it is at least conceivable that the Company would survive. In any event, gearing would remain very high for at least five years and the earliest practicable date of disposal of the NEB's shares at a profit would be mid-1985.

On the other hand the review has demonstrated that, with an additional £25 million in NEB funding, INMOS could meet the targets set for it considerably earlier and at less risk. Peak gearing would be much lower, and the earliest practicable date for disposal of the NEB's shares would be brought forward to early-1984. This option would fulfil the original aim set for INMOS since it would secure transfer of INMOS technology to the United Kingdom and would result in 75%-80% of the company's output being in this country by 1984/85. The INMOS technology centre would be preserved, and with it the prospect of a UK-based microprocessor design and manufacturing operation. However, the Board noted that sensitivity analyses done by the review show a distinct financial advantage in favour of the first UK production being sited in an assisted/steel closure area because of the Government grants and EEC loans which should be available to offset the impact of UK inflation, in particular on building costs. The relevant financial comparison is as follows:

	COMBINED CENTRE IN BRISTOL	FACTORY IN ASSISTED AREA
1984 Book Value/Share (£)	12.30	12.76
1984 PBT (£M)	29.6	30.0
Peak Borrowing (£M)	45.2	35.3
Peak Gearing	0.88	0.66

These points were brought to the attention of the Directors of INMOS. At a special board meeting called on 17th July, 1980, the directors of INMOS decided unanimously that the Company's first UK production unit should be sited in South Wales, provided that this would result in the financial assistance, including discretionary grants, outlined above. This decision was endorsed by the NEB Board on 18th July, 1980.

The NEB therefore agreed that it should confirm its request to the Government for a second £25 million of public funds for INMOS. We have looked at private sector financing possibilities and, though aiming at private investment as early as is practicable, have concluded that the prospects look unattractive at this stage and we should re-examine this when the project is more advanced. The Board hoped that, in the light of the comprehensive review it had undertaken, the Government would be able to give speedy consent to the proposal. I must emphasise that there is a need for an urgent positive decision by the Government, because if the Government decides not to grant the second £25 million the NEB and the taxpayer are currently wasting money on the INMOS facilities in the UK which would be better spent pushing ahead with a purely US company. There is therefore great urgency for a Government decision in favour of the NEB's proposals.

*Yours  
Arthur*



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10 DOWNING STREET

*From the Private Secretary*

23 July 1980

The Prime Minister has asked me to thank you for your letter of 21 July and for the copy of your letter to Sir Keith Joseph of 18 July indicating that the NEB is now supporting the INMOS management in seeking a South Wales location for the proposed UK plant.

T. P. LANKESTER

Sir Arthur Knight

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# National Enterprise Board

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BY HAND

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12/18 Grosvenor Gardens,  
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21st July, 1980.

The Rt. Hon. Margaret Thatcher, M.P.,  
Prime Minister,  
10, Downing Street,  
London, SW1.

*Dear Prime Minister*

## SOUTH WALES

On reading yesterday's press reports about events in South Wales, it occurred to me that you might find it helpful to see, in advance of the normal circulation process, the enclosed copy of a letter which I sent to Keith Joseph on Friday, following the NEB's review of the INMOS project. You will see that the NEB is now supporting the INMOS management in seeking a South Wales location for the proposed U.K. plant.

I am letting Keith Joseph know that I have written.

*Yours sincerely  
Arthur Knight*

SIR ARTHUR KNIGHT

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