



Prime Minister.

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From the Secretary of State

John Coles Esq
Private Secretary
10 Downing Street
London SW1

9 June 1982

Dear John,

FUTURE ECONOMIC DEVELOPMENT OF THE FALKLAND ISLANDS

In your letter of 26 May to John Holmes you said that the Prime Minister would like to have Lord Cockfield's comments on Mr Hunt's paper and the reactions of the Foreign and Commonwealth Office. Since you wrote, we understand that Lord Shackleton has been asked to up-date his 1976 assessment. Lord Cockfield thinks Mr Hunt's paper should provide Lord Shackleton and his team with some interesting and worthwhile ideas to follow up. I attach a paper by Department of Trade officials, which Lord Cockfield has approved, concentrating on communications and tourism.

The Secretary of State would be glad to know whether the Prime Minister would wish him to follow up any of the suggestions in the paper, especially the proposed consultancy on the prospects for tourism.

I am copying this letter to Sir Michael Palliser and John Holmes.

Yours sincerely,

JOHN RHODES
Private Secretary



Future Economic Development of the Falkland Islands:

Note by Department of Trade officials

INTRODUCTION

For the purposes of this note it is assumed that there will be an end to military hostilities once we have resecured possession of the Falklands Islands; that although regular communications with Argentina may not be restored in the foreseeable future, communications with other parts of the mainland will be possible. Without the achievement of these conditions, substantial public investment would be hard to justify and private investment is unlikely to be forthcoming.

CIVIL AIR TRANSPORT

2 Until the invasion, a weekly service by F27 or F28 aircraft (with capacity of between 50 and 75 passengers a flight) was operated between Port Stanley and Comodoro Rivadavia in Argentina by LADE, the commercial wing of the Argentine Air Force. Typically, around 25-30 passengers and some cargo were carried on each flight. It can be assumed that this service was not run as a commercial enterprise. When hostilities end, the early resumption of air services to the South American mainland will clearly be important, both as a link to the outside world for the islanders, and as a means of assisting the economic development of the islands, including tourism.

3 There appear to be two possible options: (i) short-haul flights to Punta Arenas in Southern Chile, and (ii) longer-haul flights to Montevideo or Southern Brazil (Sao Paulo or Rio de Janeiro).



4 The Punta Arenas option would be cheaper. This is because the present runway at Port Stanley could be used for service by turbo-prop aircraft (eg F27, HS748) or the smaller jets (eg F28), which are better suited than larger aircraft to likely traffic demand, at any rate for the time being. The annual operating cost of one or two services a week by an HS748 based at Port Stanley might be between £1½m and £2m, of which about £¼m might be recovered from passenger and freight charges. A charter service would be significantly cheaper, but it is doubtful whether suitable and reliable charter arrangements could be made on a long term basis in Punta Arenas.

5 There are, however, disadvantages with this option. The facilities of Punta Arenas, from the islanders' point of view, are limited, and the nearest international traffic point, for journeys to and from Europe and North America, is Santiago, 1400 miles to the North. Although there are regular daily services between Punta Arenas and Santiago, a fairly slow roundabout journey is inevitable. Moreover, the Argentines might cause trouble on the grounds that a Punta Arenas service operated within their claimed territorial limits: the state of relations with Argentina at the time would determine how great a problem this was.

6 A service to Montevideo or Southern Brazil would cost more but be a more convenient means of communication. Montevideo, Sao Paulo and Rio de Janeiro offer much better facilities than Punta Arenas. All have direct air services to North America and Europe and Sao Paulo and Rio offer a direct connection with the British Caledonian service to London. A runway of 7000 feet would be required to enable the airline to achieve an economic payload: the capital cost of this and of the provision of the necessary navigational aids etc (which may in any case be needed for defence reasons) might be of the order of £17m.



7 The annual operating cost of one service a week to Montevideo by B737 aircraft based at Port Stanley might be of the order of £3½m, of which £0.35m might be recovered from passenger and freight charges. A regular charter operation would probably also be practical if somewhat less reliable, and significantly cheaper: a single round trip service a week might have an annual cost of around £0.7m, less recoveries from passengers and freight.

8 A number of other issues would have to be resolved before any of these services could start, including:-

- (i) The other Government would have to agree.

The only Air Services Agreement between ourselves and a South American country which gives traffic rights to a UK airline on a route from the Falklands is that with Uruguay. Even in that case there is potential for dispute on the grounds that the UK/Uruguayan Agreement has not been ratified. However, the South American Governments concerned are unlikely to have serious economic objections to the service, or at any rate not ones which could not be overcome by a royalty payment. The objections, if they appear, are likely to be primarily on political grounds.

- (ii) Arrangements would have to be made for the operation of the service. Unless the service is to depend on charters from a nearby South American country, arrangements would have to be made for the service to be run from Port Stanley. This would be beyond the capabilities of the existing Falkland Islands Government Air Service. Several UK airlines have experience in managing and operating airlines in third world countries on a contract basis. One such airline,



British Air Ferries, is already showing interest in an operation at Port Stanley.

- (iii) An open-ended subsidy would have to be provided. This is inevitable: but regular air services to the outside world are important to the economic future of the Falklands. It would be desirable to explore ways of reducing the subsidy, eg by dry-leasing aircraft during the Northern summer (or suspending a charter operation), if it were acceptable to discontinue the service during the Falklands winter.

9 The conclusion is that, if the necessary improvements to the runway and other airport facilities at Port Stanley are going to be made largely or entirely in any case on defence grounds, the possibility of direct service to Montevideo or Southern Brazil looks the more attractive. If, however, the costs of the airport improvements cannot be met from the defence budget or in other ways, the Punta Arenas option would be worth further investigation.

SEA TRANSPORT

10 Prior to the invasion, the sea service to the Falkland Islands was usually provided by the AES, a Danish vessel chartered by the Falkland Islands Company. The ship made about 4 round trips a year carrying supplies for the islanders on the outward trip from UK and wool on the return. It is understood that frequently on the fourth return journey the vessel was empty. Provided that the Falkland Islands Company intend to maintain the same frequency of services once hostilities cease, there would not appear to be an urgent need to seek new capacity. The provision of additional shipping capacity may in time become necessary as the economy expands. If for any reason additional capacity is required, it may be necessary to contemplate the provision of a subsidised service. Currently a Royal Mail service vessel provides a regular service between the UK and



St Helena with the aid of an annual subsidy of about £1½m a year.

TOURISM

11 There does appear to be some potential for further development of this industry which could make a modest contribution to the economic development of the Islands.

12 The main attraction for tourists, who are likely to come in the main from North America, is the wildlife and the remote scenery. Although some hotel development is clearly required, it may well be that some tourists attracted to this kind of holiday could more easily and readily be accommodated on farms and thus provide additional income for farmers' families.

13 It seems reasonable to expect some increase in business for the "Visit Antarctica" cruises which call in on the Falklands 3-4 times a year following the increased interest in the area which the dispute has stimulated. To make the Falkland Islands more attractive to cruise tourists some investment in new hotel and other facilities will be required and labour imported for the season (only about 3 months). Inevitably most of the business provided by the tourists will go to the offshore suppliers of goods and services and special attention will need to be given to ways, including the possibility of some form of tourist tax, to ensure that economic benefit accrues to the Islands.

14 In the Department's view it will be worth seeking specialist advice from tourism consultants. A preliminary discussion has already been held with Mr Bodlender, Managing Director of Horwath and Horwath and a member of the English Tourist Board, who believes that there could well be scope for development of smaller middle quality hotels providing facilities rather than extensive service. The British Tourist Authority have also indicated to the Falkland Islands Tourist Advisory Board that they will be very happy to provide advice and assistance for a nominal fee.



AGRICULTURE

15 For the foreseeable future agriculture will remain the most important industry and must form the main basis for further development of the Islands. Mr Hunt has told the Department that a Grasslands Trial Unit funded by ODA has shown that there is potential for considerably improving sheep yields. It would seem well worthwhile tapping the considerable goodwill in New Zealand on the Falkland issue to make sure that the best expertise available is brought to bear on this problem.

16 The interest of Birds Eye Walls in purchasing surplus mutton could be followed up although it should be borne in mind that the Falkland Islands are outside the scope of the EC sheepmeat regime and would not therefore benefit from the substantial FEOGA support given to Community production. In particular, as far as MAFF are aware, there are no conventional EC or UK funds which could be used to assist the construction of an abattoir. The figure of £250,000 mentioned for this is also thought to be conservative, particularly given that long term cold storage facilities would probably also be required.

17 Sheepmeat exported to the EC from the Falkland Islands would be subject to a levy of 10 percent and a quota limit of 100 tonnes a year. Without detailed study MAFF initial reaction is that, in view of the transport problems, an operation on this scale is unlikely to be economic. New Zealand frozen sheepmeat is currently landed in this country at about £1300 per tonne. This price is enhanced by its reputation for quality which Falklands meat would probably not have.

FALKLAND ISLANDS COMPANY (FIC)

18 It seems essential that particular attention should be paid to the future of the FIC in view of the dominant role that it plays in the economic life of the Islands. The extent to which the parent company is willing to increase substantially its



investment in the Islands will need to be determined and an effort made to see whether the FIC's reluctance to sell land cannot be modified. Given the importance of agricultural development it may be worth exploring whether one of the major companies which concentrate on agricultural marketing (like Dalgety) would be interested in taking over all or some of FIC activities from Coalite, for whom they are somewhat peripheral to their main business interests.

7 June 1982