King Coal dethroned: the decline and fall of the British coal industry

The decline of the British coal-mining industry is the stuff of economic history textbooks. For a century, the industry has been contracting, and coalfields have gradually disappeared from the industrial map of Britain. The pace of decay accelerated after 1945—at the end of the war, the industry employed some 330,000 miners, and now it employs fewer than 2,000. Director at Oxera, Mike Toms, discusses his experience of the changes.

Much of the decay in the British coal industry has already been well documented: the nationalisation of the industry in 1946; the rise of natural gas and nuclear energy as alternative sources of electricity; the working-out of the most easily mined seams; the miners’ strikes of 1972, 1974 and 1984/85; the pit closure programme under Margaret Thatcher; and then the privatisation of the National Coal Board and its absorption into RJB Mining in a new commercial company which continued the closure of unprofitable pits.

But now the final chapter is being written. In April 2014 UK Coal, the last major deep-mining company in the country, announced an agreement with the government on a phased shutdown of its two remaining deep mines over the next two years. Apart from one employee-owned mine (Hatfield Colliery), and some opencast mining, Great Britain will then be entirely dependent on imported coal, both for power stations and for industry.

What brought us to this sorry position? I watched from the sidelines as a child brought up in a coal-mining community where the sight of men trudging home with blackened faces, still wearing their helmets, was a fact of all our lives. Then in 2006 I found myself with a ringside view of the issues when I joined the board of UK Coal as a non-executive director.

The company wasn’t in great shape. It had just closed its last colliery in the north-east of England, at Ellington, which had been flooded by the sea. This left six deep mines, between them providing around 7% of Britain’s power station coal. The share price stood at around £1.50. Over the next five years I saw all the risks of coal mining converge to bring the company to its knees.

Mining coal in Great Britain is inherently expensive. The coal is deep underground—up to half a mile below the surface. The seams are thin, at no more than 10 feet, and often half that. Labour is expensive and safety regulations are strict. In many other countries thick seams can be worked by scraping a few feet of soil off the surface, using cheap labour with low safety standards. Essentially, the business could survive only as long as the production cost differential was exceeded by the lower transport costs of delivering to local power stations. With such a challenging economic framework, success is bound to depend on strong finances, tight management and a healthy dose of good luck. All these were in short supply.

Geological problems caused by narrow seams forced us to mothball Harworth Colliery in 2006. In 2007 we sold Mattby Main to Hargreaves Services. It produced specialist coking coal for Hargreaves, but the company couldn’t make the mine profitable, and it closed suddenly in 2013. In 2009 we merged Welbeck Colliery in Nottinghamshire, which was becoming worked out, with nearby Thoresby.

Mining is a very cash-flow-driven business, and over the same period we suffered severe disruption to production, from both fatal accidents underground and ‘face gaps’, which emerge when one area of the mine, or ‘panel’, is worked out and fresh tunnels have to be cut. Workers and equipment then need to be installed in the new area and production restarted. When a mine stands idle, it bleeds cash at a frightening rate. Detailed plans to minimise these gaps were drawn up, but the gaps were always longer than anticipated. Part of the reason lay in industrial relations. Extended face gaps provided the workforce with opportunities to earn bonuses to recover lost time and start the new faces, although, in winning these concessions, the miners were eroding the financial viability of the operation. The management regularly briefed the unions on the parlous state of the business, but I never felt that the workforce fully appreciated the extent to which their actions put their
own livelihoods at risk. Bitterness from the 1980s still prevailed and, at some mines, NUM (National Union of Mineworkers) members would still not work with UDM (Union of Democratic Mineworkers) members.

The situation was exacerbated by two distinctive features of our labour economics. The first was that most of the workforce were aged over 40, and many were in their 50s. Many did not have to consider a future beyond their own retirement. The second was that fear for their pensions was low. Although the company had a pension liability out of all proportion to the size of the business—over £130m by 2010—the unions were all aware that the Pension Protection Fund would guarantee the workers 90% of their full pensions even if the company collapsed.

Mining is dangerous and this is made worse when individuals take risks. In five years, five UK Coal miners died underground in different pits, each incident having its own unique causes. Each death caused disruption to the mine as well as distress to the families and fellow miners. The company had to invest time and money in improving the safety culture.

Coal is traded internationally on a very liquid spot market and it is normally priced in US dollars. The dollar price fluctuated widely and variations in the exchange rate added to this. Cash-flow problems had led the company to reduce its exposure to market prices by entering into fixed-price contracts with only four UK electricity generators. Competition drove these contracts down to survival prices and meant that the company could not build up reserves when spot prices were high. Production difficulties meant that contracted volumes could not always be delivered, which led to extensions to contract lock-in periods.

Up to 2008, the company’s balance sheet was underpinned by its large holdings of land with potential for housing in the north of England. This holding had attracted interest from property investors, which resulted in a rapid run-up in the share price to a high of around £6. The company found itself with one active property investor, Peel Holdings, owning 29.9% of the business and claiming a place on the board. Unfortunately, just as planning consents were being won for development, the housing market collapsed and creditors started closing in.

Meanwhile, the government had been developing its energy policy, and had concluded in the 2006 Energy Review that it was important to retain a strong GB mining industry. What action did the government take to secure that industry? There was to be no financial support, but there would be a ‘Coal Forum’ to discuss mining matters.

A distress rights issue was successfully launched in 2009 at 75 pence per share, generating £100m in funds which should have stabilised the company. Disastrously, this was followed immediately by a series of production failures, including an extended outage when another death underground required a review of safety equipment and processes. The whole cash pile evaporated in a few months. Three profit warnings in six months destroyed the company’s standing with shareholders and made it entirely reliant on the continuing support of its bank.

Bizarrely, over the same period, just down the road from UK Coal’s headquarters in Doncaster, Richard Budge, Chairman of Coalpower, was attempting to restart deep mining at Hottfield Colliery in Sheffield. The mine reopened in 2006, supported by Russian finance, but went into administration in 2010 and was eventually transferred to an employees trust. The mine has also struggled with operational disruption.

Although fate conspired against UK Coal during this period, the management and the board had to shoulder their share of the responsibility. The company’s chief executive, an experienced American mining engineer, retired in 2009, and the focus on the property portfolio led us to promote the property director to replace him. In retrospect, we probably underestimated the importance of continuing to employ specialist leadership to focus on the mining business until it was too late.

In early 2010 we saw a possible way out. Merger talks started with Hargreaves. But when these collapsed, and with the share price down to around 30 pence, we were called to account by our largest shareholder and the bank. The chief executive and chairman both left and the remaining non-executive directors set out to find a tough, energetic new executive chairman to grab hold of the company and turn it around.

The appointment of Jonson Cox was welcomed, and the share price picked up to around 40 pence. The new chair set out with vigour. He made his view very clear in an uncompromising characterisation of the previous three years of unacceptable performance. In his first annual report, he assured shareholders that they deserved a better return. He soon replaced a number of directors (the author included). Consultants were hired to expose the company’s cost inefficiencies, the annual pay increase was cancelled, and the defined-benefit pension scheme was closed. Negotiations were started with the unions to reduce labour costs, such as bonuses and allowances. The particular focus was Daw Mill Colliery in Warwickshire, which was the company’s most productive mine, but also the one with the most entrenched labour issues.

Despite these initiatives, the old problems resurfaced. Almost immediately there was another long face gap at Daw Mill, then another death underground. Some costs were cut, but no sustainable resolution with the unions emerged. The coal price also started to fall just as the company began to move away from its old fixed-price legacy contracts towards a more market-based pricing strategy. In March 2012 the company announced that, as a result of the failure to agree cost savings with the unions, consultations would be opened on the closure of Daw Mill Colliery. At the end of 2012 the company completed a reorganisation under the new corporate identity of Coalfield Resources, separating the liabilities of the mining and property operations. This left ownership of the UK Coal mining business effectively in the
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dependent on imports for coal-fired electricity.

What conclusions do I draw from this?

First, no matter how bold the management, deep mining is a very high-risk business, unsuited to heavily geared financial structures.

Second, geology and economics mean that deep mining in Great Britain is an inherently unprofitable business at current or recent coal prices.

Third, entrenched historical industrial relations can still defy economic reality for extremely long periods.

Finally, government policy on security of supply means nothing unless it is matched with timely and positive action.

Mike Toms

Fate dealt the final blow. The end was brought forward when an underground fire in February 2013 closed Daw Mill earlier than planned. In July 2013 the company entered a ‘pre-pack’ administration, in which Coalfield Resources surrendered all responsibility for the mines and became solely a property company. This reorganisation allowed UK Coal to keep the Kellingley and Thoresby mines in operation, but by the start of 2014 it was becoming clear that even these were no longer viable. In April 2014 the company announced that it would close Kellingley and Thoresby immediately unless the government stepped in with emergency aid to allow an orderly run-down over the following two years. The government finally engaged with the company; the result is that, by the end of 2015, Great Britain will be almost entirely

hands of the Pension Protection Fund, while the property business was shared 25/75 between the shareholders and the Pension Protection Fund. Another round of management changes took place. The share price fell to around 3 pence. The shareholders were left waiting for their better returns.


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