

SECRETPRIME MINISTERBRITISH LEYLAND

This note follows up some of the points raised at Sir Robert Armstrong's meeting yesterday, which I attended, and suggests some lines of thought for your meeting on 2 April.

1. WHAT ARE THE POSSIBLE OUTCOMES FOR BL?

1.1 There is a conflict as regards objectives and the respective views of BL's prospects, between Michael Edwardes and his Board, on one hand, and the Government on the other.

1.2 The Government View

1.2.1 Colleagues seem fairly certain that BL will not recover to a point where it ceases to be a continuing worry to Government. The fear is that the next crunch point cannot be very far away and that, if we take no action, the Plan will be withdrawn when there is little time and money left to decide what to do.

1.3 Edwardes' View

1.3.1 Understandably, Edwardes still maintains that BL can recover and prosper. Although we have assumed that the BL Board would withdraw the Plan as soon as it appeared unattainable, Edwardes has in fact admitted, in his letter of 18 March, that the Plan will not be attained in full this year, but the Board has not proposed its withdrawal. Since any "drift" away from the Plan is likely to happen bit by bit, it is in practice very difficult for non-executive directors to choose a particular point at which to stop accepting Edwardes' assurance that they should continue.

1.0.2 The Edwardes view boils down to this: "Government must not start looking for buyers because that would leak in the closed motor industry world. This would precipitate collapse and undermine the recovery programme. Therefore, Government cannot do anything about selling BL until the Plan is withdrawn - ie BL is approaching collapse. But in any case, I believe that BL will recover, so Government will have a better opportunity to sell BL as a whole, if it wants to, in a year or two." The difficulty is that Edwardes is reaching for a better outcome for BL and for himself, at the risk of heavier penalties, for Government, if he fails. His objectives are not wholly aligned with ours and his view of the likely outcome is also different.

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1.3.3 Edwardes believes that extensive collaboration may be the key to BL's future. We have some doubts about this, as it is difficult for a large company to control its own future if it is simply acting as the peripheral agent of a number of large autonomous collaborators. But this needs further thought. I am not sure how large a part it plays in his recovery strategy. (His public references to collaboration do, however, provide a good cover for talking to potential buyers.)

1.3.4 We cannot say that judgment about the likely outcome, or about the point at which the Plan should be withdrawn, "is a matter for the BL Board, not Government". Government is the owner and foots the bill and cannot leave that judgment entirely to the people it has hired to run it.

2. HOW DO WE VALUE THE OUTCOMES?

2.1 | Recognising that Edwardes' assessment of the different outcomes is different from ours, we have to look at each outcome to be clear what we are going for.

2.2 There are four possible outcomes:

- (1) Sale of BL, complete.
- (2) Orderly break-up and disposal (perhaps following failure to do (1) above).
- (3) Disorderly break-up and disposal (following withdrawal of the Plan).
- (4) BL recovers.

2.3 Which is the best outcome? And which is the worst acceptable outcome? We doubt whether outcome (4) - BL recovery - is in fact the best possible outcome, unless it was so spectacular and so firmly-based that BL moved, in the space of a couple of years, to being fully comparable with its major international competitors. This seems inconceivable to us. We think the best outcome would be sale of BL as a whole. The worst outcome, to be avoided at all costs, would be a disorderly break-up, followed by a "fire sale". This is likely following belated withdrawal of the Plan, with time, money and market confidence rapidly running out. The worst acceptable outcome would be orderly break-up and disposal, with time and money in hand.

3. CHOICE OF STRATEGY

- 3.1 Our real concern is to minimise the downside. We therefore want a strategy which minimises the chance of outcome (3) - disorderly break-up and sale.
- 3.2 At present, we have only two options. We can either take no action (apart from the possible use of an expert to prepare the ground internally, which is not essential and could be dangerous) and simply wait for BL to turn-around or for the Plan to be withdrawn; or we can decide now to look actively for a buyer for the whole of BL, recognising that this could leak and force us towards an early break-up and disposal. It may help to display these two strategies against the different outcomes, as follows:

Note. I am not suggesting for a moment that such different decisions can be made "by members." How this sort of approach can help to structure the problem in one's mind.

OUTCOMES STRATEGIES	(1) BL sold entire	(2) Orderly break up and sale	(3) Disorderly break-up and sale
A. No Immediate Action	Unlikely	Unlikely	Probable
B. Try to Sell BL Now	Possible	Likely	Possible

Strategy B gives the highest chance of (1) and the lowest chance of (3)

I have left outcome (4) - BL recovers - off this chart.

3.3 Strategy A - no immediate action - implies the following:

- It effectively rules out the chance of a sale of BL as a whole (though this would be possible if our view proves wrong, and BL does get better, instead of worse).
- It increases the chance that eventual sale will be a fire sale, following the withdrawal of the Plan.
- By delaying, it makes it likely that there will be fewer possible buyers who have not already made other plans.
- It does not prevent BL's turning around under its own steam if it can.

3.4 Strategy B implies the following:

- It effectively rules out the chance of BL recovering under its own steam, under Government ownership.
- It increases the chances of an orderly break-up and disposal rather than a fire sale.
- It offers the best chance of selling BL as a whole.

3. Which should we choose? The answer is that you choose strategy A if you're an optimist, about BL, strategy B if you're a pessimist.

4. QUESTIONS WE NEED TO ASK

- 4.1 We need to ask a number of questions before we can decide which route to take. For example:

- (1) Is it necessary, or even possible, to attempt to sell BL secretly? Have there been many - or any - cases of large companies changing hands without anybody knowing? Are we clear in our minds about what a "collapse of confidence" really means if such plans leaked?
- (2) What is the evidence for the view that the Board would resign if we decided to sell the company before the Plan had been withdrawn? They must presumably be on the brink of withdrawing it themselves.
- (3) What would the union reaction be to the sale of BL, whenever and in whatever form it happens? Would we be able to explain that our objective in selling BL is to avoid closure and high unemployment, not to precipitate it?
- (4) If we take no action now (strategy A) and the Plan was later withdrawn, could we find ourselves having to prop up BL with Government money while we look for buyers, and thus appear to be doing the very U-turn we said we would not do?
- (5) Is Edwardes' idea of multiple collaboration likely to succeed? Are we underestimating the possibilities there?
- (6) Could BL insure itself against the risk of a dealer network collapse during sale negotiations? Could it make the dealers an offer they couldn't refuse to keep the network in being over that period?

5. HOW TO PROCEED

- 5.1 Whatever the conclusions of the 2 April meeting, it would be very helpful for colleagues to discuss this whole problem with Michael Edwardes and also with someone like Sir Henry Benson (as Sir Robert Armstrong has suggested). I agree with Sir Robert's view that hiring an expert to do preparatory work for a sale is not the right next step.

5. Such a discussion would itself be part of the process of coming to a conclusion about whether we want to start seriously looking for a buyer now or whether we want to wait until the Plan is withdrawn. If our preference is for the former, then the sooner those discussions with Edwardes and Benson take place the better; if it is for the latter, there is less urgency, but such discussions would certainly be helpful.

6. CONCLUSION

- 6.1 I do not think that there is a middle course between deciding to sell BL outright and setting that process in motion immediately, on the one hand; and simply waiting until BL either succeeds or fails, on the other. If we still believe that BL is quite likely to succeed, then it is too early to act. If we do not, then it will soon be too late. There is no way of proving in advance which view is right, and the temptation to do nothing is therefore strong. As I understand it from the meetings we have had, you, Geoffrey and Jim (but perhaps not yet Keith?) are virtually convinced that BL will in the end fail and are therefore anxious to act early to prevent the worst outcome.



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