LCC(78)174

SECRET

COPY NO. 17...

BRITISH LEYLAND

1. Background

Following the Ryder report in 1975, the Government made an offer for the existing shares of British Leyland (the cost of the resulting acquisition was £46 million) and subscribed £200 million in equity capital to a rights issue by the company. All these shares were vested in the National Enterprise Board to give it a 95 per cent shareholding in British Leyland.

The Ryder report recommended that British Leyland would need an additional £1000 million (in current prices) from public funds between 1975 and 1982. Loans of £100 million (£70 million from National Enterprise Board and £30 million under Section 8 of the 1972 Industry Act) were authorised by the Government in July 1977. £50 million of this was released to British Leyland in September, while the remaining £50 was held back - at the company's request - because of BL's failure to meet its targets.

2. Leyland's Corporate Plan

The National Enterprise Board published a report on Leyland's latest Corporate Plan on April 3rd 1978. The product and manufacturing plan for BL cars stresses the need to provide coverage of the main sections of the car market, but with a smaller number of models and components than those in current use. There are, however, some major changes in detail and emphasis from the Ryder plan.

a) a remodelling and re-direction of the model originally planned to replace the Mini;

b) a higher priority to be given to improving the Land Rover and Range Rover models and to increasing capacity for their production;

c) an attempt to provide an early updating of existing models in the medium car range, pending the introduction of a new model;

d) reaping the maximum benefits from the Jaguar and Rover Saloon car range;

e) a fundamental change of philosophy over monitoring BL's performance. The NEB criticise their own approach of linking the provision of cash to the company's meeting its targets; claim it has engendered a gratutious lack of confidence in the company; and now support the Edwardes line that a commitment of a large sum - largely unconditionally - is essential now, as part of the "act of faith" for which the Chairman has called.

The manufacturing plan concedes the need for some attempt at matching capacity with demand. The forecast for 1978 is a net job loss of 10,000 (excluding the effects of the Speke closure).

3. Future Financing

BritishLeyland has asked the NEB for £450 million in 1978. Cash provision in the form of equity is sought by the British Leyland Board in order to restore the strength of their balance sheet which currently shows an unsatisfactory debt: equity ratio of 75:25

£450 Million equity will produce a ratio of 49:51. Leyland [illegible] the need for an equity base sufficient to sustain an adequate private sector borrowing capability.

The NEB has accepted Leyland's request for funds and is prepared to provide £300 million in 1978 provided its borrowing powers are enlarged. The NEB proposes that the remaining £150 million shall be made available under Section 8 of the 1972 Industry Act, and the Government agrees with this. £275 million of this money will be needed to re-finance temporary loans from the private sector. The remaining £400 million would be made available subsequently making a total of £850 million for the period covered by the Corporate Plan (1978-81). The form of additional finance will be decided in November 1978 after an updated Corporate Plan and Budget for 1979 have been considered by the NEB and the Government.

The Leyland Board has suggested that in the same period it should be able to generate from its own resources a comparable sum to that provided by the taxpayer (£850 million). In addition it expects, with its strengthened balance sheet, to be in a position to obtain extra finance from the private sector. These sums of money would be used to finance an investment programme of some £1300 million and to provide working capital.

4. Future Performance Targets

The NEB accepts the opinion of Michael Edwardes, Chairman of British Leyland that "support now is an act of faith". It recommends that new finance should not be subject to specific conditions about improvements in industrial relations and productivity. The Leyland Board has strenously argued that longterm investment programmes cannot be turned on and off by reference to day to day industrial relations performance. Instead there will be a review in November 1978 of the company's success or otherwise in achieving its targets. In accepting the NEB's recommendations for future financing Mr Eric Varley, Secretary of State for Industry said:

> "If events show a serious risk that the Plan's objectives cannot be achieved, then the Government with the company and the NEB will have to consider the options: and the Government would have to accept the financial consequences of any change of plan that it might then agree with the NEB"
>
> (Hansard 3rd April 1978)

This sounds ominously like a recognition that further funds may be necessary over and above the £850 million that has already been requested by Leyland. It also raises the possibility that a number of major financial decisions can and should be deferred until that review. It certainly diminishes the case for giving more money now to the NEB itself.

Conspicuously absent from the Corporate Plan are ambitious targets on production, market share and productivity. Michael Edwardes has indicated that the company is initially aiming at a market share of around 25-30 per cent with annual production of around 800,000 cars. This compares with the Ryder target of 33 per cent market share and 1 million cars. The efficiency improvements are forecast to cause the output per man per year to rise by 18.5 per cent from 5.40 in 1977 to 6.40 in 1978 and in later years to over 8.0. But the Leyland board accepts that:

> "greater improvements than those forecase are essential if the company is to be fully competitive",

5. The NEB's Stewardship

Neither the NEB nor the Department of Industry have ever been in the habit of providing adequate information about British Leyland. The latest documents are no exception to this pattern. The statistics quoted have been very carefully chosed and presented with no historical comparisons of performance earlier than 1976, even though the company was in the Government's hands well before that date; No details of targets and outturns; measures of output for which comparable statistics are probably unobtainable; and so on.

In an important sense the proposals the Government is now making to Parliament reflect not only on the problems, prospects and financial needs of British Leyland but those of the NEB as well. The NEB has been in charge of BL's rescue since (at the latest) its creation. It has failed, on its own admission, in every respect. The management it appointed has had to be fired, the company's performance has got worse, not better, and a new start is having to be made. Furthermore the NEB's failure is, naturally, threatening to deprive it of money it would like to use for other purposes. It is the NEB, not Leyland which is seeking the bulk of the financial assistance Parliament is being asked to grant on Monday. And as usual Parliament is being asked to vote vast sums at 5 days notice on the basis of grossly inadequate information. It should be noted that as far as can be judged the NEB could advance to British Leyland the £300 million which it and the Government have accepted BL should have without infringing its financial limit, As Mr. Varley's statement made clear. ("This would take the NEB close to its present financial limit of £700 million").

6. The Orders

a) An order has been laid before the House raising the NEB's financial limit from £700 million to £1,000 million. This increase of £300 million is less than the £850 million total of NEB funding BL has asked for. However, if the NEB has some £300m of spare resources now, a further increase of £300 million would assure it some £600 million out of the £850m required.

b) An order for affirmative resolution under Section 8 of the Industry Act 1972 to provide the remaining £150 million required by Leyland in 1978.

7. The Options

a) Approve both orders. This might win some votes in marginal seats in the Midlands. Equally it might lose some among non car worker voters in these seats who are far from happy at heavy subsidies being continually paid out to a company whose previous performance had been so disastrously bad. It would be difficult to reconcile unqualified support for the orders with our stance as guardian of the taxpayers' interests.

b) Approve the Industry Act order, but oppose the extended NEB limits. This would enable us to combine backing Michael Edwardes and BL with the exercise of a considerable degree of restraint on taxpayers' money and a picture which symbolises a tough but reasonable attitude to the NEB in the light of its past failures. It might make us much less vulnerable to Labour criticism. Mr. Varley's written answer makes it clear that the NEB does not need an increase in its financial limit in order to provide Leyland with the £300 million. Therefore the order is in effect providing the NEB with more money not because it is essential if British Leyland is to get the £300 million it wants, but rather to preserve the NEB's capacity to continue its other activities. No doubt the NEB will say that without this increase their non Leyland activities would have to be severely cut back. But is is after all Party policy that this should happen. The NEB should be able to provide at least part of the money by selling off some of its assets. Our line could be "Yes to a successful and competitive Leyland, No to Bennery". They might also be able to borrow against their portfolio of companies and increase their resources that way* We would need an effective presentation of our case to make it clear that our target is the NEB as much as British Leyland, and that Monday's votes are about the NEB rather than British Leyland.

(c) Approve the NEB order but oppose the Industry Act order. There would be little reason for doing this.

(d) Vote against both orders. This would be a posture consistent with our previous warnings about the likely failure of the Ryder plan and would reflect our deepseated antipathy to throwing good money after bad. But it would give Labour a further propaganda stick with which to beat us and would not be uniformly popular in the Party.

(e) Abstain on both orders. This would enable us to express strongly our concern at the large amounts of taxpayers' money involved without giving the Labour Party a stick to beat us with in the 'motor' seats.

In this context we should not forget the significance of the autumn review of British Leyland's revised corporate plan and business plan for 1979. It is for consideration whether we might not argue that it is only appropriate to consider the NEB's case for further funding for onward transmission to British Leyland - if ever - after that review, in the light of the consideration of the proposals for fixing British Leyland's "financial duty" which Mr. Varley has already said will be for decision at that time. Why should one vote such large sums for NEB/British Leyland before one even knows the return that will be earned on them? The NEB has only stated that a return of no higher than 10 per cent by 19[illegible] would be realistic.

8. Political Points

Long after the arguments in the debate have been forgotten, a simple impression of our votes will be remembered. The Labour Party will see to that. We need, therefore, during the debate and more important, after it, to articulate strongly our position and its justification. Some of the points we could usefully make are:

( ) We want to see a successful and profitable British motor car industry. Michael Edwardes has a proven record as a successful manager and he should be given the chance to succeed.

---

* This is a highly technical issue which is still being investigated.

(2) We welcome the recent improvement in performance by Leyland. But two months' figures and a couple of good speeches by the Chairman do not make a summer. Leyland's performance over the last few years has been disastrous. We still need more solid evidence of progress before caps can be thrown in the air and large sums used. Hence we might be right to wait till the Autumn review before passing judgement. In the meantime the NEB can provide what money is required without recourse to Parliament.

(3) Britain has backed and is backing Leyland. But Leyland must now back Britain in every area: better management, a sustained increase in market share, production and productivity and, last but certainly not least, fewer strikes.

(4) Although eventually Leyland is supposed to generate internally sums matching those provided by the taxpayer, none of the £450 million needed for 1978 is to be provided either by the NEB or by Leyland from their own resources. Why should not the NEB sell off some of its assets to provide at least part of the money - or Leyland too - for example its special products and truck divisions? Even if the latter were sold for nothing the taxpayer would be saved the expense of satisfying the financial needs of these profitable divisions of the company. The task of raising this money would be transferred to the private sector.

(5) What will the Government do if things go wrong? The criteria for failure in any case are far from clear. What guarantee has the taxpayer that Leyland will not be back, cap in hand, for more money in two years' time? It has always been a critical weakness of the Government's position that it has no clear idea of when the taxpayers' liability would end; that the NEB is equally deficient; that no clear criteria of success or failure are set, let alone adhered to. While Michael Edwardes may dislike the publicity which the linkage of cash assistance to performance caused in the past, the company has the rememdy to that problem in its own hands - improve performance.

Conservative Research Department,
24 Old Queen Street, London, SW1.

ANR/PRR/MHM
5.4.78