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R. Lakosov.

COMMERCIAL SECRET

P.071

MR WILE

I am content to embark on the same \$750 million suggestion - we all know the difficulties of what Prime Minister

True, 1987

cc: Sir Kenneth Berrill  
Mr Mountfield

Shall we proceed as suggested at X below?

ROLLS ROYCE

It is impossible but it is the most hopeful suggestion I have seen yet. Provided a high confidence is retained we can go ahead with his study <sup>also Charceller's Advice Plag B. D. Clark.</sup>

Flag A

Sir Keith Joseph's minute to the Prime Minister of 13 July canvasses the possibility that GEC might buy the whole of Rolls Royce, sell back to the Government the aero-engine business assets and then have a management contract with the Government to supervise the aero-engine business "with penalties and rewards dependent on performance." Sir Keith Joseph acknowledges that the proposal may not be feasible and that work will be necessary to clarify this. Before starting such work however he wants to have the Prime Minister's permission to inform Sir Kenneth Keith, the Chairman of Rolls Royce, and Sir Leslie Murphy, the Chairman of the NEB, of the GEC proposals.

2. There is little doubt that the suggestion made by Sir Arnold Weinstock should be examined - any proposal to dispose of Government-owned assets is welcome - and it follows that Sir Keith Joseph should be given the permission he seeks. At the same time it will be necessary to have a good deal more information before the Government can take decisions. Among the questions which spring to mind are:-

Would Sir Kenneth Berrill be able to advise on the merits of the proposal?

(a) How much might GEC pay for the non-aero engine business of Rolls Royce and is there a better-paying alternative?

(b) How practical is it to devise a "penalties and rewards" contract for GEC management in a situation where Rolls Royce will be losing a lot of money on the aero-engine business (unless the exchange rate falls) for which Government will continue to be responsible?

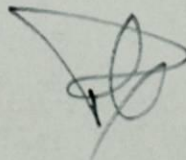
This does cover all points of (a).

(c) What is the significance of the proposal that GEC should first buy the aero-engine business and then sell it back to Government? There would not seem to be much point in this manoeuvre unless they hope to sell back for more than <sup>they</sup> pay.

(d) How profitable is the Rolls Royce non-aero engine business? What rationalisation might follow from GEC acquisition? Are there likely to be any particular problems for the Government, eg in relation to competition policy?

(e) What is the <sup>2</sup>inwardness of the apparent intention to integrate part of GEC's present activities with RR as a separate heavy electrical/gas turbine/aero-engine business which might later be put on the market as an independent company? On the face of it this cuts across the purity of the idea that GEC would manage the aero-engine business owned by the Government. Clarity is needed to make sure that the Government has adequate control over the public money which would continue to go to the aero-engine segment of the new organisation.

3. There could well be other problems in working out a practical solution. On the other hand if a realistic and defensible operation is possible which would reduce public expenditure and obtain an adequate price for Rolls Royce, there is much to commend the idea in principle. The need is for a good deal more information. As we understand it, Sir Keith Joseph is due to meet Sir Leslie Murphy on Monday evening to discuss the sale of some other NEB assets. The immediate question is whether he should be allowed also to float this idea in strict confidence or whether the proposal needs to be discussed by Ministers collectively first. But to do this might lose valuable time and the Prime Minister might think it preferable to allow Sir Keith Joseph to begin, without commitment, exploration both with Sir Leslie Murphy and Sir Kenneth Keith and simultaneously to ask the Secretary of State for Industry, in consultation with the Chancellor of the Exchequer, to prepare a quick appraisal of Sir Arnold Weinstock's ideas for consideration by Ministers in E(DL).



P Le CHEMINANT

13 July 1979