

SUBJECT

SECRET



re B7

bc Mr Walters
u Hoskyns
u Wolfson
made

10 DOWNING STREET

From the Private Secretary

13 January 1981

As you know, the Prime Minister held a meeting yesterday afternoon to discuss the Government's approach to BL's request for funding of their corporate plan. The following were present in addition to your Secretary of State: The Chancellor of the Exchequer, Mr. Tebbit, Sir Robert Armstrong, Mr. Ibbs, Mr. Hoskyns and Mr. Wolfson. They had before them John Hoskyns' note of 8 January, as well as the various papers which had earlier been circulated to E Committee.

Sir Keith said that, in commercial terms, it would be right to refuse any further funding of BL. At best, their prospective rate of return on a CCA basis was 1% by the late 1980s - which might just be enough to finance new models at that stage. The much more likely outcome was that BL would have to continue to depend on Government financing and guarantees for their investment in new models. It was true that BL's forecasts were now more conservatively based than they had been in the past and Sir Michael Edwardes had done a great deal to improve the internal performance of the company; but the chances of success were still very slim. On the other hand, Ministers had to consider the wider implications of withdrawing support. The component industry would be badly hit in the short term, and there would be massive PSBR costs (though he understood that the Chancellor no longer felt that these constituted a decisive argument against early closure). There was also the political aspect. If the Government refused to provide further support, this might be good for its overall credibility and in many quarters would be popular; on the other hand, it might also be deeply resented insofar as, to many people, it appeared that BL's management and workforce had begun to perform better. From a political standpoint, he was marginally in favour of withdrawing support. But if Ministers collectively took the opposite view, there seemed no real alternative to supporting the plan in full. Annual funding would still be subject to performance checks, but he did not feel it would be possible to "drip feed" the company, or for example to omit the financing of the LC10: either of these courses would immediately undermine the confidence of the dealer network and BL's volume sales would collapse.

The Chancellor said that his preliminary view was that, taking into account the wider aspects, the Government should continue to support BL. He did not think that the economy would adjust rapidly enough to take up the slack caused by early closure to make the latter a viable option. Nor did he think it would be acceptable for only about a quarter of UK car sales to be provided from domestic sources. Also, in the short run, financing the plan would involve no greater cost to the PSBR than closure. But further work needed to be done on the size and type of car industry that the UK needed. And if it was decided to fund BL's plan, the essential aim should be to put the Company into a better position for a merger with another company and/or to enable it to dispose of some of its operations.

In discussion, it was suggested that the prospect of BL returning to profitability was virtually zero. Although Sir Michael Edwardes and his management team had brought about some improvements, the Company had nonetheless signally failed to meet its targets. Moreover, whereas Sir Michael had indicated a year ago that he would withdraw the plan if the Company failed to meet its targets, he had done no such thing. It was unlikely that he would do so in the future. If the Government was going to fund the plan, it would be as if the Government were providing finance for political reasons to a welfare organisation. At the very least, the Government should insist on BL disposing of the more profitable parts of its business such as BL vehicles and landrover. Sir Michael Edwardes had been asked to pursue this course last year, but had failed to deliver. This must not be allowed to happen again. Moreover, it was essential to avoid anything like a full commitment to the plan. It was too easy simply to accept Sir Michael's view that there either had to be a commitment of over £1 billion or else BL would collapse. The possibility of a "middle way" should be explored, including the possibility of not funding the LC10.

Against this, it was argued that a partial commitment would involve even greater expense than supporting the plan in full. In that case, BL would without any doubt whatever collapse before long and in the meantime more money would have been spent. Moreover, the criticisms of BL management were not fully justified. They had not withdrawn the previous year's plan because BL had been thrown off course largely by external, rather than internal, factors. If the new plan were invalidated by failure to meet internal performance criteria, there were reasonable grounds for believing that the plan would be withdrawn. Despite all the problems at BL there was an economic case for continuing to support them: the immediate unemployment consequences and the ripple effect on other industries of not doing so would be too great. Even if there were a case in principle for withdrawing support, closures in the steel and shipbuilding industries should have higher priority; and it was not politically possible to achieve all at once.

In conclusion, the Prime Minister said that more work needed to be done on refining the options. In particular, the possibility of a "middle way" - including not funding the LC10 - should be urgently examined. This further work should be done by the No. 10 Policy Unit, the CPRS, your Department and the Treasury and a report brought back to Ministers as soon as possible. If it was eventually decided to provide further support to BL in some form or other, she would wish to see Sir Michael Edwardes to impress upon him the Government's objectives.

/ I am sending

SECRET

- 3 -

I am sending a copy of this letter to John Wiggins (HM Treasury), Gerry Spence (CPRS) and David Wright (Cabinet Office).

TPL

Ian Ellison, Esq.,
Department of Industry.