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Submitted to 13
PM 20/12
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DESKBY 201800Z

FM WASHINGTON 201620Z DEC 81

TO IMMEDIATE F C O

TELEGRAM NUMBER 3872 OF 20 DECEMBER 1981.

MY TELNO 3862: BSC/KAISER.

1. LLOYD CUTLER (SENIOR PARTNER IN THE LAW FIRM WILMER, CUTLER AND PICKERING AND FORMER COUNSEL TO PRESIDENT CARTER) TELEPHONED MINISTER YESTERDAY MORNING, AS KAISER'S COUNSEL, TO DISCUSS BSC'S POSSIBLE ACQUISITION OF KAISER. CUTLER HAD EARLIER IN THE DAY DISCUSSED IT AT LENGTH WITH SECRETARY BALDRIGE. CUTLER SUBSEQUENTLY CALLED AT THE EMBASSY AT HIS OWN SUGGESTION. I SAW HIM BRIEFLY AND HE THEN GAVE THOMAS AN ACCOUNT BOTH OF HOW THE DEAL WOULD LOOK FROM KAISER'S POINT OF VIEW AND OF HIS TALK WITH BALDRIGE.

2. CUTLER CONFIRMED THAT KAISER HAD DEFINITELY DECIDED TO SHUT DOWN THEIR LIQUID STEEL CAPACITY, SITUATED AT OAKLAND, CALIFORNIA, 40 MILES INLAND AND SUBJECT TO STRINGENT ENVIRONMENTAL REGULATIONS, THEY WERE NO LONGER ABLE TO PRODUCE SLAB STEEL COMPETITIVELY. NOR WOULD IT BE WORTH MAKING THE HEAVY INVESTMENT THAT MIGHT ENABLE THEM TO DO SO. THEY WOULD THEREFORE NEED TO BUY IN BASIC STEEL SLAB TO KEEP THEIR FINISHED STEEL OPERATIONS GOING. THIS THEY FULLY INTENDED TO DO. CUTLER ASSERTED (AS MORGAN HAD DONE YESTERDAY WITH BALDRIGE) THAT NO U.S.-PRODUCED SLAB COULD COMPETE ON THE WEST COAST WITH IMPORTED SLAB, GIVEN THE HIGH COST BOTH OF BASIC STEEL PRODUCTION HERE AND OF INLAND OR INSHORE TRANSPORT. KAISER WOULD THEREFORE HAVE NO CHOICE BUT TO IMPORT IT. THE MAIN COMPETITIVE SOURCES AT PRESENT WERE THE FAR EAST (JAPAN OR KOREA) OR EUROPE (UK OR SWEDEN). THIS WAS WHY KAISER HAD APPROACHED BSC IN THE FIRST INSTANCE.

3. CUTLER SAID THAT THE KAISER MANAGEMENT WOULD WELCOME BSC'S BID TO TAKE THEM OVER. WITHOUT A LINK OF THIS KIND, THEIR FUTURE WOULD BE UNCERTAIN. FROM THE INDUSTRIAL AND MANAGEMENT POINT OF VIEW BSC'S BID WOULD BE GREATLY PREFERABLE TO THE ONLY ALTERNATIVE BID THAT WAS ON OFFER. (HE MENTIONED HILLER, WHO HAD ORIGINALLY OFFERED DOLLARS 50 PER SHARE AND MOVED UP TO DOLLARS 54. THE KAISER BOARD, HE SAID, WERE LOOKING FOR A BID "SOMEWHERE NORTH OF DOLLARS 60".) CUTLER BELIEVED THAT THE TRADE UNION INVOLVED, AS WELL AS LOCAL INTERESTS IN CALIFORNIA, WOULD ALSO REACT FAVOURABLY TO A TAKEOVER BY BSC SINCE THIS WOULD OFFER THE BEST PROSPECTS FOR THE PRESERVATION OF JOBS.

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4. FROM BSC'S POINT OF VIEW, CUTLER SAW THAT THE ACQUISITION OF KAISER REPRESENTED A GREAT OPPORTUNITY FOR BSC. THOMAS ASKED HOW CUTLER WOULD RATE THE LONG TERM VIABILITY OF A BSC/KAISER PARTNERSHIP IN THE U.S. MARKET. CUTLER PREDICTABLY THOUGHT THAT ON PRESENT PRICE AND PERFORMANCE FORECASTS IT WOULD BE EXCELLENT. BUT EVEN IF THESE FORECASTS PROVED WRONG OVER THE MEDIUM TO LONG TERM, THE SHORT TERM PROSPECTS WERE SO GOOD THAT BSC WOULD HAVE GOT ITS MONEY OUT. THE CASH POSITION OF KAISER AND ITS DISPOSABLE COAL ASSETS WOULD HELP TO ENSURE THIS.

5. CUTLER HAD FOUND THAT BALDRIGE'S MAIN CONCERN WAS THE REACTION OF U.S. INDUSTRY. IF THE STEEL INDUSTRY WAS DISPOSED TO ACCEPT THE DEAL, BALDRIGE DID NOT THINK THE U.S. GOVERNMENT WOULD OPPOSE IT. CUTLER RECOGNISED THAT THERE WAS A RISK THAT OFFICIALS MIGHT RECOMMEND AGAINST ANOTHER TAKEOVER BY A FOREIGN NATIONALISED CORPORATION. BUT IN ADDITION TO ELF/AQUITAINE, THE GOVERNMENT HAD RECENTLY LET THROUGH THE ACQUISITION OF SANTA FE BY THE GOVERNMENT OF KUWAIT. UNLESS THE U.S. STEEL INDUSTRY CREATED AN UNHOLY ROW, BALDRIGE'S VIEW, AS RELAYED BY CUTLER, WAS NOW THAT THE U.S. GOVERNMENT SHOULD NOT BE A PROBLEM.

6. THE KEY PROBLEM WILL BE THE U.S. STEEL INDUSTRY. CUTLER SHARED BALDRIGE'S VIEW THAT BSC SHOULD NOW TAKE SOUNDINGS WITH THE TOP PEOPLE IN THE U.S. STEEL INDUSTRY. CUTLER WOULD BE IN TOUCH TODAY WITH GERARD (CHIEF EXECUTIVE OF KAISER) AND MCGREGOR TO ADVISE THAT THEY SHOULD GO EARLY NEXT WEEK TO SEE RODERICK (U.S. STEEL) AND ONE OR TWO OTHERS TO EXPLAIN THE PROJECT AND SEEK A REACTION.

7. IN CUTLER'S VIEW THE WAY TO PRESENT IT WOULD BE TO SHOW THAT THE ACQUISITION OF KAISER WOULD SERVE AS A KIND OF PERFORMANCE BOND FOR BSC, OR A GUARANTEE OF "GOOD BEHAVIOUR". WITH A STAKE OF THIS SIZE IN THE U.S., BSC COULD SIMPLY NOT AFFORD TO RUN THE RISK OF INCURRING ANTI-DUMPING OR COUNTERVAILING ACTION. ACCORDING TO CUTLER, BOTH BALDRIGE AND MCGREGOR THOUGHT THIS APPROACH WOULD BE PERSUASIVE.

8. THOMAS ASKED WHETHER THERE WAS NOT SOME RISK THAT IF BSC'S PRICES FOR SLAB, ALBEIT INTERNAL TO THE MERGED COMPANY, WERE THOUGHT BY U.S. STEEL PRODUCERS TO REFLECT A SIGNIFICANT ELEMENT OF SUBSIDY, THEY MIGHT ATTRACT COUNTERVAILING ACTION. CUTLER POINTED OUT THAT IT WOULD NOT BE NECESSARY TO RUN THIS RISK. BSC COULD RAISE THEIR SLAB PRICES (FOR INSTANCE IN THE EVENT OF A TRIGGER PRICE FOR SLAB BEING INTRODUCED) AND IF NECESSARY RUN KAISER AT A LOSS, BUT STILL MAKE A PROFIT OVERALL. IN ANY CASE, HE ARGUED THAT ONCE BSC'S UK PLANT WAS OPERATING AT A HIGHER LEVEL OF CAPACITY UTILIZATION ITS PRICES SHOULD BE HIGHLY COMPETITIVE WITHOUT BEING SUBSIDIZED.

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9. CUTLER SUGGESTED THAT GIVEN THE UNCERTAINTIES FOR HMG, A PRUDENT WAY TO PROCEED MIGHT BE TO AUTHORIZE BSC TO ENTER INTO NEGOTIATIONS FOR A MERGER AGREEMENT WITH KAISER. UNDER U.S. PRACTICE SUCH AN AGREEMENT WOULD CONTAIN A VARIETY OF WARRANTIES AND "OUTS", FOR EXAMPLE IN THE EVENT THAT THE U.S. GOVERNMENT RAISED OBJECTIONS TO THE MERGER. THE MAIN CONDITION ON KAISER'S SIDE WOULD BE THAT THE DEAL SHOULD BE APPROVED BY A MAJORITY OF SHARE HOLDERS. THIS KIND OF AGREEMENT WAS MORE THAN A LETTER OF INTENT. IF NONE OF THE CONTINGENCIES PROVIDED FOR AROSE, THE AGREEMENT WOULD BE BINDING. BUT IT PROVIDED BOTH SIDES WITH AN ELEGANT AVENUE FOR WITHDRAWAL IN THE EVENT OF THEIR CONDITIONS NOT BEING MET.

10. CUTLER WAS OF COURSE SPEAKING IN THE INTERESTS OF KAISER WHOSE BOARD WOULD LIKE THE TAKEOVER TO TAKE PLACE. HE IS A SKILLFUL AND EXPERIENCED ADVOCATE, WELL KNOWN TO MCGREGOR AS WELL AS TO THE OTHERS CONCERNED.

11. ADVANCES TO BRIDGES (DESKBY 201800Z VIA RESIDENT CLERK) AND SIR P CAREY, MANZIE AND MURRAY (DOI) (DESKBY 210900Z).

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12A M. Snow. Mr. Whitmore to see

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ZZ WASHINGTON
GRS 444
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FM FCO 181300Z DEC 81
TO FLASH WASHINGTON
TELEGRAM NUMBER 1959 OF 18 DECEMBER

YOUR TELEGRAMS NOS 3826 AND 3847: BSC/KAISER

1. THIS QUESTION WAS CONSIDERED FURTHER AT A MEETING OF MINISTERS LAST NIGHT. SAMUEL C BUTLER OF CRAVATH SWAINE AND MOORE (ATTORNEYS IN NEW YORK) AND JOHN A MORGAN (SMITH BARNEY) WHO HAVE BEEN CALLED IN TO ADVISE THE DEPARTMENT OF INDUSTRY, WERE PRESENT FOR PART OF THE TIME.
2. IT WAS AGREED THAT, WITHOUT PREJUDICE TO HMG'S FINAL DECISION, AN ENQUIRY SHOULD BE MADE OF THE US SECRETARY OF COMMERCE PERSONALLY TO ASCERTAIN HIS VIEWS ABOUT THE PROPOSED ACQUISITION. AS MORGAN IS WELL-KNOWN TO SECRETARY BALDRIDGE IT WAS DECIDED THAT HE WOULD BE THE BEST PERSON TO APPROACH THE SECRETARY. BUT MINISTERS ALSO CONSIDERED THAT THE MINISTER (COMMERCIAL) SHOULD ACCOMPANY HIM.
3. MORGAN IS RETURNING TO THE USA TODAY AND WILL BE INFORMED OF THIS DECISION ON ARRIVAL. HE WILL BE ASKED TO CONTACT THOMAS AND TO MAKE THE APPROACH TO SECRETARY BALDRIDGE AS SOON AS POSSIBLE.
4. THE POINTS ON WHICH WE PARTICULARLY NEED BALDRIDGE'S VIEWS ARE THOSE IN A, C AND D OF YOUR TEL NO 3826. SPECIFIC QUESTIONS WHICH SHOULD BE COVERED IN THE CONVERSATION INCLUDE :
 - (A) WHAT WOULD BE THE EFFECT OF AN ACQUISITION OF THIS SIZE (INITIAL COMMITMENT OF DOLLARS 200 MILLION BY BSC, AND LOAN OF SAME AMOUNT RAISED BY BSC IN USA) ON US VIEWS OF THE STANDING OF THE TWO CORPORATIONS IN THE US STEEL MARKET?
 - (B) WHAT WOULD BE THE PROSPECT OF ANNUAL IMPORTS OF L.5 MILLION TONNES OF SLABS DO TO THE EXISTING STEEL IMPORT REGIME?
 - (C) WHAT IS THE RISK THAT NEWS OF THE MERGER WILL CAUSE ANTI-DUMPING SUITS AGAINST BSC, DESIGNED TO PREVENT THE

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CORPORATION FROM STRENGTHENING ITS POSITION IN THE MARKET?
(D) WOULD THE DEAL RENDER BSC MORE VULNERABLE TO COUNTERVAILING
ACTION, FOR THE SAME REASONS?

AGAINST THE BACKGROUND OF THESE SPECIFIC QUESTIONS WE ALSO WANT
TO KNOW BALDRIDGE'S OVERALL JUDGEMENT ON

(I) HOW THE ACQUISITION WOULD BE VIEWED BY THE US INDUSTRY, AND
(II) WHAT WOULD BE THE LIKELY ATTITUDE OF THE US ADMINISTRATION -
POSITIVE, ADVERSE, OR NEUTRAL?

5. THE COMMENTS IN YOUR TELEGRAMS HAVE BEEN HELPFUL IN
CONSIDERING THE QUESTION HERE. MINISTERS ACCEPTED THAT THE
VIEWS OF BSC'S OWN ATTORNEYS IN WASHINGTON WOULD BE VERY RELEVANT,
AND THE DEPARTMENT OF INDUSTRY HAVE SUGGESTED TO BSC THAT THEY
INSTRUCT CUNNINGHAM ACCORDINGLY. BUT THEY ALSO THOUGHT THAT,
GIVEN SECRETARY BALDRIDGE'S RESPONSIBILITY FOR THE TPM AND HIS
FREQUENT CONTACT WITH LEADERS OF THE US STEEL INDUSTRY, HIS VIEW
OF THE LIKELY EFFECT OF THE PURCHASE WOULD BE VALUABLE. BUT
THERE IS LITTLE TIME TO SPARE AND THE MEETING SHOULD TAKE

PLACE IN THE VERY NEAR FUTURE

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Pass on
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office
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GRS 870
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FM WASHINGTON 190105Z DEC 81
TO IMMEDIATE FCO
TELEGRAM NUMBER 3862 OF 18 DECEMBER

*I think they
confirms the
wisdom of our
decision
MS*

SECRET

Prime Minister

12

(2)

Even if Mr MacGregor got a
green light now (last para), could
we be sure the arrangements would be
unchallenged over the years during which
they'd have to run if employment at
Ravenscroft
Blawieon
were to be
safeguarded?

YOUR TELNO 1959: BSC/KAISER

1. JOHN MORGAN (SMITH BARNEY) AND MINISTER CALLED ON SECRETARY
BALDRIGE THIS AFTERNOON AND SPENT AN HOUR AND A HALF WITH HIM.
BALDRIGE LISTENED INTENTLY WHILE MORGAN EXPLAINED THE BASIS OF
THE PROPOSED ACQUISITION AND SUMMARISED THE QUESTIONS WHICH THE
PRIME MINISTER HAS ASKED HIM TO TRY TO CLARIFY (ESSENTIALLY THOSE
SET OUT IN YOUR TELEGRAM UNDER REFERENCE).

MS 19/12

2. BALDRIGE'S ATTITUDE WAS SYMPATHETIC BUT CAUTIOUS. HE IDENTIFIED
THREE MAIN PROBLEMS IN THE COURSE OF THE DISCUSSION. FIRST, THE
TIMING COULD NOT BE WORSE. HE WAS HAVING GREAT DIFFICULTY AT PRESENT
HOLDING THE US STEEL INDUSTRY BACK FROM FILING 90 OR SO ANTI-
DUMPING AND COUNTERVAILING ACTIONS AGAINST EUROPEAN STEEL PRODUCERS.
BSC WERE CERTAINLY AMONG THE TARGETS. BALDRIGE HIMSELF HAD IMMENSE
RESPECT FOR THE STEPS WHICH THE BRITISH GOVERNMENT AND BSC WERE TAK-
ING TO RESTORE THEIR POSITION. BUT BSC'S OUTPUT WAS GENERALLY
REGARDED HERE AS AMONGST THE MOST HIGHLY SUBSIDISED OF ALL. THIS
APART, THE US STEEL INDUSTRY FELT THAT THEY HAD ALREADY BEEN TAKEN
FOR A RIDE TWICE ON THE TRIGGER PRICE MECHANISM (AND BALDRIGE
HIMSELF CLEARLY HAD SOME SYMPATHY WITH THIS VIEW). THEY WOULD NOW
BE CLOSELY WATCHING THE OUTCOME OF THE US GOVERNMENT'S CURRENT DISCU-
SSIONS WITH THE EUROPEAN COMMISSION TO SEE WHAT KIND OF UNDERTAKINGS
WOULD BE FORTHCOMING ABOUT RESPECT FOR THE QUOTE INTEGRITY UNQUOTE
OF THE TRIGGER PRICE MECHANISM. IF THESE WERE NOT SATISFACTORY, THE
US INDUSTRY WOULD UNQUESTIONABLY GO AHEAD WITH A SERIES OF ANTI-
DUMPING AND COUNTERVAILING ACTIONS. BALDRIGE CLEARLY FELT THAT IF A
DEAL INVOLVING THE ACQUISITION OF KAISER BY BSC WERE ANNOUNCED IN
THIS ATMOSPHERE, IT WOULD BE ANYTHING BUT HELPFUL.

3. SECOND, BSC WAS A NATIONALISED COMPANY. THE FACT THAT IT WAS ALSO
WIDELY BELIEVED TO BE SUBSIDISED MADE MATTERS WORSE. FOREIGN
TAKEOVERS WERE NOW SUBJECT TO EXAMINATION IN A SUBCABINET COMMITTEE.
IF IT WAS A QUESTION OF A PRIVATE SECTOR COMPANY
TAKING OVER KAISER, HE DID NOT THINK THERE WOULD BE ANY PROBLEM.
BUT THERE HAD BEEN INCREASING CONCERN ABOUT THE TAKEOVER OF US
NATIONAL RESOURCES BY FOREIGN NATIONALISED ENTERPRISES. HE MENTIONED
PARTICULARLY ELF/AQUITAINE'S TAKEOVER OF TEXAS GULF LAST SUMMER,
WHICH HAD CAUSED A CONSIDERABLE ROW. BALDRIGE SAID THAT THE ADMINIS-
TRATION WERE PROBABLY WORKING TOWARDS A POLICY WHICH WOULD AS A
GENERAL RULE EXCLUDE TAKEOVERS OF US COMPANIES BY FOREIGN NATIONAL-
ISED ENTERPRISES. A PROPOSAL NOW BY BSC TO TAKEOVER KAISER MIGHT
PRECIPITATE A DECISION. PRIVATE SECTOR COMPANIES IN THE US INCREASIN-
GLY FELT THAT IT WAS UNFAIR IF THEY WERE TRYING TO COMPETE IN THE
MARKET PLACE WITH COMPANIES BACKED BY THE FULL WEIGHT OF FOREIGN

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GOVERNMENT RESOURCES. BALDRIGE WAS NOT CERTAIN HOW THE ADMINISTRATION WOULD RESPOND TO THIS MOOD. NOR WAS HE SURE THAT IF IT DID IT WOULD NECESSARILY EXCLUDE THE DEAL ENVISAGED BY BSC. BUT HE CLEARLY SENSED SOME DANGER OF THIS.

4 THIRD, THE VOLUME OF STEEL INVOLVED WOULD MEAN A SIGNIFICANT INCREASE IN THE LEVEL OF IMPORTS IN THE US FROM BSC. AT PRESENT IMPORTS OF SLAB WERE RELATIVELY SMALL AND CAME MAINLY FROM CANADA. THEY WERE NOT SUBJECT TO THE TRIGGER PRICE MECHANISM BUT IF QUANTITIES WERE TO INCREASE, THIS COULD BE CHANGED. IN ANY CASE, IF THE MAJOR STEEL PRODUCERS FOUND THAT THEIR INTERESTS WERE BEING DAMAGED BY AN INFLUX OF SLAB FROM BSC, IT WOULD BE OPEN TO THEM TO LOOK AT THE CASE FOR INSTITUTING AN ANTI-DUMPING OR COUNTERVAILING PETITION. WITHOUT GOING INTO THE CASE IN GREATER DETAIL, HE COULD NOT BE SURE WHAT THE REACTION OF THE INDUSTRY MIGHT BE.

5. AFTER MORE THAN AN HOUR OF MORGAN'S PERSUASIVE ARGUMENTS AND THOMAS'S QUESTIONS, BALDRIGE, THOUGH MUCH INTRIGUED, STILL SEEMED TO FEEL IN HIS BONES THAT THE US INDUSTRY WOULD NOT MUCH LIKE THE DEAL. HE DID NOT THINK THE US GOVERNMENT, WHICH WAS STRONGLY SYMPATHETIC TO MRS THATCHER'S POLICIES AND OBJECTIVES, WOULD NECESSARILY WANT TO BLOCK IT, AT LEAST IN THE ABSENCE OF A CLEAR POLICY AGAINST TAKEOVERS BY FOREIGN NATIONALISED COMPANIES. BUT THE PROPOSAL WOULD HAVE TO BE CAREFULLY EXAMINED AND BALDRIGE WAS NOT PREPARED TO FORECAST HOW A DECISION MIGHT GO. HE THOUGHT MUCH WOULD DEPEND ON THE REACTION OF THE INDUSTRY. HIS ADVICE THEREFORE WAS THE MACGREGOR, WHO WAS WIDELY KNOWN AND RESPECTED AMONG THE CHIEF EXECUTIVES OF THE MAJOR US STEEL CORPORATIONS, SHOULD TAKE DISCREET SOUNDINGS OF ONE OR TWO OF THEM. THE MOST IMPORTANT IN HIS VIEW WOULD BE RODERICK (US STEEL) AND DELANCY (REPUBLIC, AND CHAIRMAN OF THE AMERICAN IRON AND STEEL INSTITUTE). IF MACGREGOR COULD GET A GREEN LIGHT FROM THEM, BALDRIGE THOUGHT HE WOULD FEEL REASONABLY CONFIDENT THAT NOT MUCH DAMAGE WOULD BE DONE. WITHOUT THAT HE CLEARLY THOUGHT THAT FOR ALL ITS ATTRACTIONS, THE SCHEME WHICH HAD BEEN OUTLINED TO HIM WAS FROUGHT WITH A GOOD DEAL OF RISK.

6 ADVANCE TO BRIDGES (FC), SIR P CAREY (DOI),
MANZIE (DOI), MURRAY (DOI).

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