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UNDER PART V OF THE  
1987 BANKING ACT



Treasury Chambers, Parliament Street, SW1P 3AG  
01-270 3000

21 October 1988

P R C Gray Esq  
PS/Prime Minister  
10 Downing Street  
LONDON SW1

Prime Minister

You will wish to see.

RCG  
21/10

Dear Paul

mt

The Chancellor has asked me to write to you about a tricky banking supervision issue which has arisen this week.

The Prime Minister may recall that the New Zealand company Equiticorp acquired a 61% shareholding in the merchant bank Guinness Mahon during 1987. The Bank of England have for some time felt that Equiticorp are not fit and proper shareholders within the meaning of the Banking Act; there are doubts both about their financial stability and their integrity. The upshot is that Equiticorp are now trying to sell their shares at the insistence of the Bank of England. The original deadline for the sale - 15 October - has already passed.

Over the past months several foreign banks have expressed a general interest, but in the event only one firm bid has so far been received. This is from a Japanese City bank, Tokai. The Governor has told the Chancellor that the Bank will agree to this bid, unless the Treasury gives notice of intention to lodge a formal objection under the reciprocity provisions of the 1987 Banking Act. This would be the first Japanese acquisition of a British merchant bank, and as such it would be seen as a significant step. It may also revive interest in the Tokyo Stock Exchange position - they have still not publicly agreed to admit BZW to membership. (The Prime Minister will recall that she raised this issue with Prime Minister Takeshita earlier in the year.)

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The Chancellor has therefore considered very carefully whether it would be right to block this bid. He has concluded that such a step would not be in the national interest (as required for the exercise of the Treasury's Banking Act powers). This is for two reasons.

First, there is a very strong prudential case for allowing the bid to proceed. Equiticorp must divest themselves of their shares, as soon as possible. And the Japanese are offering a very good price, together with satisfactory assurances on such matters as management independence. The Bank have no prudential concerns about them: Tokai have had a sizeable London branch since 1963 and they are known to be in good standing with the Japanese authorities.

There is still a chance that a substantial Swedish bank, PKbanken, may put in a bid, but this looks increasingly unlikely, at least at a price which comes close to matching the Japanese offer. If Equiticorp were forced to sell its shares at a demonstrably inferior price (or were subjected to the formal sanctions specified in Section 26 of the Banking Act) the Government could expect strong protests, and conceivably legal challenge, from Equiticorp's shareholders and creditors (quite apart from any Japanese complaints).

Second, the Chancellor believes there are other more suitable levers available with which to apply pressure on the Japanese over the Tokyo Stock Exchange. Moreover, we have talked recently with Sir Martin Jacomb about the BZW position. He is hopeful that progress will be made after the imminent appointment of a new Tokyo Stock Exchange President (whom he will be arranging to see personally as soon as he can). Meanwhile, BZW's business in Tokyo is quietly developing and he has told us he is anxious that nothing should occur to disturb relations with the Japanese. If this later proves over-optimistic, we could, if we chose, apply pressure on the Japanese by the terms in which we respond to a number of Japanese regional banks who are known to be anxious to establish branches in London, and whom the Bank of England are still quietly keeping at bay.

The Bank need to express a view about the general acceptability of the bid by close of play on Monday. If, contrary to expectations, the Swedish bank comes forward with a firm expression of interest over the weekend, at an attractive price, the Chancellor will wish to review the position on Monday. However, in the absence of such a bid, the Chancellor agrees with the Governor that the right course is to allow the Japanese offer to go ahead.

*Yano*  
*John*  
pp. A C S ALLAN

Principal Private Secretary



*see pm*

10 DOWNING STREET  
LONDON SW1A 2AA

*From the Private Secretary*

24 October 1988

The Prime Minister was grateful for the information in your letter to me of 21 October about the Equiticorp shareholding in Guinness Mahon. The Prime Minister has noted the course of action proposed.

Paul Gray

Alex Allan, Esq.,  
H.M. Treasury.

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