

~~MARKET SENSITIVE~~

PRIME MINISTER

BRITISH AEROSPACE (BAe)

I mentioned to you on Monday that I had that day been told by Sir Tin Pearce of BAe that he had had an approach from Peter Laister of Thorn-EMI to merge that company with BAe.

2 We hold 48% of the ordinary shares of BAe; and at the time of its privatisation in February 1981 undertook that "HM Government has also made it clear that, in any event, it intends to retain a shareholding conferring more than 25% of the voting rights ordinarily exercisable in general meetings". Because of our holding and our commitment, careful thought will have to be given to what we should do, in the event that the Thorn-EMI proposal turns into a formal bid. We may have to react very quickly, as a formal bid would become notifiable under Stock Exchange rules. It is clearly right for us to prepare our position in advance. If the bid were to be contested, we should come under pressure as to what attitude we wish to adopt towards our shares: whether to support the bid, remain neutral, or - in

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advance - make clear to Thorn-EMI that we should block any bid. We must also expect to be pressed on what steps we intend to take to ensure that what in the past has been regarded as an important defence capability remains in British hands. I should welcome Michael Heseltine's view on the continuing importance of the defence considerations. I suggest he should be brought into the discussions of the proposal. The reason for our commitment to a 25% shareholding was to enshrine in BAe's articles of association provisions protecting it from foreign control. We shall need to consider what should be our attitude towards a residual shareholding in a larger merged company; or whether alternative means should be sought to prevent undesirable foreign control.

3 On general industrial grounds, my initial assessment is that there is a great deal to be said for the proposed merger. Thorn-EMI is a company less vulnerable to the long cycles of development which BAe experience; and its cash flow would strengthen BAe. The Thorn-EMI management, which would clearly dominate in any merged company, would provide a more aggressive and commercial approach, and much needed improvement in financial control. For these reasons I see industrial advantage in what is proposed. The overlap



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between the companies is limited; and on my present knowledge I should not consider a reference to the Monopolies and Mergers Commission to be necessary. However, were any bid by Thorn-EMI to flush out counter-offers - for example, from GEC - a reference might well become desirable.

4 BAE were not able to tell me what had attracted Thorn-EMI to its interest in a merger, other than the obvious discrepancy between the two companies' P/E ratios. BAE, whose tactics towards Thorn-EMI are to delay any substantive discussion until after the BAE AGM on 15 May, have not probed this (or any other) aspect of the proposal. I therefore do not know what Thorn-EMI's plans would be towards the civil aircraft programmes now being carried on by BAE. I see this as one of a number of important points to be taken up with Laister.

5 I therefore see the informal approach which has taken place as presenting us both with problems and with what might be an opportunity for a significant strengthening of our industrial structure. Clearly, we need to know more. I intend, therefore, subject to your agreement, to explore with Laister, in discussion next week, what attitude Thorn-EMI intends to adopt towards the BAE business, and in

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particular towards the Civil Aircraft programmes, and report back subsequently. In the meantime, I believe it right to preserve an absolutely neutral attitude towards the Government shareholding; and to set in hand some investigation of the practicality of preserving a merged company from undesirable foreign control, other than through maintaining a significant shareholding.

6 I am copying this minute, which is the only written record of the discussions which I have had with Sir Tin, to Nigel Lawson. I should be grateful if its confidentiality could be very tightly guarded indeed.

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2 May 1984

Department of Trade and Industry

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