81-2 £620- (450 / 335) [Sp. 520] ∴ £100 - to 45 [illegible] / 52

82-3. £370-. (Sp 260]

A

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£990 [800] Not until 1985 - commercial profit - i.e. full year's [illegible]

Level of profit / 6.. - only one element.

- charge = [illegible]

- depreciation.

JU679 (£190 m. + £150)

PRIME MINISTER

1987.

BL's 1983 CORPORATE PLAN

83-4-5 - to continue to fund losses.

An interdepartmental group of officials, under the chairmanship of Mr Gordon Manzie, a Deputy Secretary in my Department, has been studying BL's 1983 Corporate Plan. The Treasury, the Scottish Office, the Department of Trade, the Department of Employment and the CPRS participated in the group. A copy of their report is attached at Annex A to this minute.

2 The review of the 1983 Plan has taken place against the backcloth of the understanding on privatisation and the future funding of BL which was reached between the Government and the BL Board last summer and was recorded in Michael Edwardes' letter to me of 4 August (a copy is at Annex B to this minute). In essence, BL undertook with our approval to present in the 1983 Plan a strategy for full privatisation which offered visible progress in that direction within the next two years; and not to seek further Government funds for the maintenance of the business after March 1984, subject to agreement by the Government to provide not only the remainder of the £990 million of equity capital already agreed but also such part of the further £150 million previously envisaged as was not offset by the estimated proceeds of privatisation in the financial year 1983-84. In the event, BL have reduced their requirement to £100 million in anticipation of these proceeds, which will not be received until later.

3 The Manzie Group's conclusions, which were unanimous, are set out on pages 70-77 of the report. Briefly, the main ones are that BL as a whole is still on the course towards profitability which has been plotted in previous years' Plans, although prospects and performance vary between the different businesses;

and that the privatisation strategy included in the Plan, although its detailed implementation has not yet been worked out, presents reasonable prospects for visible progress towards privatisation in the next two years. The Group recommends that the 1983 Plan should be approved, and that BL's request that £100 million of equity should be made available in the financial year 1983-84, over and above the £150 million or so of the £990 million previously agreed which is likely to be rolled over to that year, should be agreed. Although provision is sought for £250 million in 1983-84, there is a possibility that the experience of the last two years will be repeated, and that some of this will slip into 1984-85. I would not regard this as a problem. Because of the timetable for drawing up the public expenditure programme, no PES provision was made for these amounts, which will have to be found from the Central Reserve. I did, however, alert the Chief Secretary to this expected requirement during my PES bilateral with him in September.

4 I agree with the advice which officials have given in the report. However, serious problems have still to be dealt with in the Leyland and Austin Rover Groups, and the Government will clearly need to monitor closely their performance and prospects in 1983. We shall also need to keep closely in touch with progress towards implementation of the privatisation strategy for all the businesses. In the case of Austin Rover, there are no prospects of full privatisation on present projections of the company's balance sheet. This is not because of a deterioration in the company's performance or prospects but because, as we have always known, the volume cars business cannot be viable on its own in the near future. Progressive extension of the collaboration with Honda, preferably with the introduction of a minority equity stake by Honda, offers the best chance of reducing and eventually ending Austin Rover's dependence on the Government. However, I think it is important that, as part of the review of the options for this business which is to take place in the coming months, BL themselves and Government officials should study whether there might be any ways in which the Government's exposure under the

Varley/Marshall assurances to creditors could be first limited and then reduced as the business returns to profitability. Though I am by no means sure that such means can be found, I have asked that a study should be put in hand. I would propose to include in the letter conveying the Government's approval of the 1983 Plan some paragraphs reflecting these considerations and setting out the basis on which approval is given, on the lines of those in Annex C to this minute.

5 I should be grateful to know whether you and other colleagues agree that we should approve BL's 1983 Corporate Plan and the associated funding requirement. If you do agree, I would propose to make a written statement to the House soon after the Christmas recess.

6 I am copying this minute to the Chancellor of the Exchequer, the Secretaries of State for Scotland, Trade and Employment, to Mr John Sparrow and to Sir Robert Armstrong.

PJ

P J

11 January 1983

Department of Industry
Ashdown House
123 Victoria Street

ANNEXA

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OFFICIAL GROUP ON BL

REPORT ON BL'S 1983 CORPORATE PLAN

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I. INTRODUCTION

1.1 On 26 January 1981, the then Secretary of State for Industry announced the Government's decision to approve BL's 1981 Corporate Plan and "to fund the first two years of the Plan, including the first phase of the LC10 programme - that is, £620m in 1981-2 and £370m in 1982-3 - subject to regular monitoring by the BL Board of progress in achieving the Plan". In agreeing to fund two years of the Plan, rather than the normal one, Ministers accepted BL's arguments that a longer-term settlement was needed in order to maintain the confidence of dealers and management up to the launch of the LM10 in spring 1983. The 1981 Plan did, however, envisage the provision of a further £150m equity during 1983-4, although it made no formal request for this to be provided by Government. In approving the Plan, the then Secretary of State, while not excluding the possibility that these funds might be provided by Government, expressed the hope that BL would be able to raise them from the private market.

1.2 The 1982 Plan endorsed the strategy outlined in the 1981 Plan, with the exception of the strategy for the Leyland Group which had accumulated substantial losses during 1981. (For the Leyland Group the Plan proposed a radical restructuring in order to restore viability.) In particular the Plan reaffirmed that in addition to the £990m equity requested for the two years 1981-3 there would be a need for a further £150m in 1983-4, although once again there was no formal request for this to be provided by Government. The Official Group which considered the Plan concluded that the strategy proposed for the Cars, Unipart and Land Rover Groups offered reasonable prospects for continued recovery along the lines foreseen in the 1981 Plan, and that the strategy for the Leyland Group, while admittedly subject to substantial risks, offered some prospects of recovery and should be approved subject to especially close monitoring. Ministers endorsed this view and the Minister of State for Industry announced on 22 December 1981 that the Government had approved the 1982 Plan and reaffirmed the Government's commitment to providing £620m equity in 1981-2 and £370m in 1982-3. (In the event only £520m equity was required in 1981-2, and Ministers agreed in March 1982 that the remaining £100m should be rolled over and would be available if required in 1982-3.)

1.3 Early in 1982 the Government proposed that BL should raise at least part of the equity needed after March 1983 by selling Land Rover to the private sector in 1983 as the first step in the process of returning the whole of the company to the private sector. The Board accepted the long-term objective of returning BL to the private sector but argued that selling Land Rover in 1983 would be harmful to the rest of BL and would probably result in a delay in the privatisation of the remaining companies. After a series of discussions between Ministers and the BL Board Sir Michael Edwardes wrote to the Secretary of State on 4 August setting out the understanding which had been reached on the privatisation issue and on the future funding of BL. Mr Lamont replied on 6 August confirming that the Government's position was properly reflected in Sir Michael's letter. According to this exchange of letters, BL undertook:

a) to present in the 1983 Corporate Plan a strategy for full privatisation which offered visible progress in that direction within the next two years by such means as the sale of minority equity stakes in BL's more profitable business; and

b) not to seek further Government funds for the maintenance of the business after March 1984, subject to agreement by the Government to provide not only the remainder of the £990m already agreed but also such part of the £150m previously envisaged as was not offset by the estimated proceeds of privatisation in the financial year 1983-84.

1.4 The 1983 Plan therefore includes, in addition to the usual projections for each of the constituent business, a section describing how each business might be returned to the private sector. It is however too early to assess the proceeds of privatisation, and it is in any event unlikely that significant proceeds would be available to the company during 1983-84. In order to fulfil the commitment at 1.3(b) above, however, BL has reduced its request for a further £150m of equity over and above the £990m already agreed, and is now seeking only another £100m.

1.5 The 1983 Plan therefore raises three main issues, which are considered in the remaining chapters of this report. The first is whether, on the basis of BL's performance in 1982 and the latest projected results for the future, there are reasonable prospects for the recovery of the company to viability. This question is considered further in Chapters II and III. The second question is whether the privatisation strategy outlined in the Plan fulfils the commitments in Sir Michael Edwardes's letter of 4 August, and this is addressed in Chapter IV. These questions lead to the third, namely, the implications of the 1983 Plan for BL's funding, and more particularly the extent of Government funding which should be agreed. This is considered in Chapter V.

1.6 If it is agreed to provide further funds to BL over and above the £990m already notified to the European Commission, it will be necessary to notify the Commission of the decision. It would also be necessary to inform the Commission if payment of any part of the £990m already notified were to be deferred until after March 1983, since their earlier approval related to the provision of £990m over the two financial years 1981-82 and 1982-83.

II BL PERFORMANCE IN 1982

2.1 The performance of BL as a whole during 1982 has been reasonably encouraging, in a very difficult world and UK economic climate. For the first time in four years, the company is expected to meet its PBIT target. This performance reflects different fortunes amongst the Groups, with only Cars Group individually performing better than Plan.

2.2 The following table sets out the latest forecasts of the main performance indicators for the four principal Groups making up BL. In order that comparisons can be made with the figures in the 1982 Corporate Plan, these projections are on the old four-Group basis, showing Cars Group as a single entity (rather than split into Jaguar and Austin-Rover Group). These figures are based on BL's forecasts in the Corporate Plan, although latest forecasts are referred to where significant differences arise. The main difference lies in cashflow, which is now forecast to be £82m less than shown in the 1983 Plan and £115m less than in the 1982 Plan (principally as a result of a £32m further reduction on forecast capital expenditure).

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		Cars	Unipart	Leyland	Land Rover	BL*
Revenue	(£m)	1740	335	797	438	2978
Better/(worse) than Plan		(62)	(64)	(122)+	(38)	(302)
PBIT	(£m)	(105)	11	(29)	8	(134)
Better/(worse) than Plan		17	(2)	(38)+	(4)	11
Retained Earnings	(£m)	(181)	4	(41)	(10)	(301)
Better/(worse) than Plan		43	(2)	(24)	(5)	19
Cashflow in/(out)	(£m)	(320)	(10)	(130)	(46)	(524)
Better/(worse) than Plan		14	(12)	(33)+	(6)	33
Capital expenditure	(£m)	142	11	58	40	267
(Lower)/Higher than Plan		(21)	2	1	(8)	(49)
Sales volumes	(000)	423	NA	49	66	517
Better/(worse) than Plan		(26)		(3)	(3)	(32)
Market share UK	(%)	18	NA	14	NA	NA
Better/(worse) than Plan		(2)		(2)		
Manpower	(000)	48	5	31	14	103
Lower/(higher) than Plan		4	1	-	2	9

*Includes other companies and central adjustments, not shown separately

+The effects of these shortfalls on the total BL figure were mitigated by the inclusion in the Plan of central contingency provisions against such shortfalls, of £52m revenue, £40m PBIT, £55m cash flow.

2.3 Although market sizes were generally greater in 1982 than was foreseen in the 1982 Plan, conditions in the vehicle industry were still depressed, and this, together with the relative strength of sterling for a large part of the year, has led to fierce price competition. BL's inability in some cases to achieve planned revenues and market shares must be seen against these market conditions, in which very few non-Japanese vehicle makers are showing satisfactory results. BL's control of costs has, on the other hand, again proved excellent; and there have been substantial gains on the industrial relations front, with the current pay round satisfactorily completed and the general atmosphere much calmer than last year.

2.4 Only the Leyland Group fell seriously short of its own hopes for PBIT- though the projected shortfall is largely contained by the central contingency included in the 1982 Plan. Market share has been well below budget, but against this there are some encouraging signs: facility rationalisations and the introduction of new models have been achieved as planned; the unsuccessful January strike, whilst harmful in the short term, ended with acceptance by the workforce of substantial manpower reductions; and the "benchmark" performance on model profitability, manpower, costs and quality is at or close to budget. It is important to note that much of the shortfall arose in overseas operations, which although consolidated into the Leyland Group do not rely on the centre for funding.

2.5 Performance on cashflow shows a similar pattern to 1981, with Cars Group expected to be better than Plan, and the others worse (although with that of Leyland Group more than offset by the central contingency). On latest forecasts, the cash outflow is expected to be £82m less than is shown in the 1983 Plan. A major feature of this is a £32m reduction in the forecast capital expenditure. Capital expenditure is therefore expected to be £81m less than Plan, and £135m less than the budget, which included a provision for expenditure deferred from 1981. Of this accumulated shortfall, BL are now estimating that about £95m will be rolled forward into future years. BL have however stressed that this rephasing of capital expenditure will not result in any delay to product launch dates, because of a reduction in the lead time of a number of projects.

2.6 During the year, £260m of equity funding was provided to the company leaving £210m of the funding available for 1981/82 and 1982/83 so far unissued. £202m of medium term bank loans were also drawn down during 1982, partly offset by a reduction in short term borrowings.

2.7 Brief assessments of the performance of the main businesses follow. More detail is given in Annex 1.

Cars Group

2.8 Despite a competitive UK market, in which all manufacturers have had to spend money on discounts to dealers and on marketing campaigns, BL have kept total costs within Plan levels, and considerably lower than in 1981. This has enabled them to show a slightly better than Plan PBIT despite a small revenue shortfall. In a larger than expected UK market, BL had a lower than Plan market share: the major models, Metro and Acclaim, performed well within sectors (for instance, Metro outsold the Fiesta), but these sectors declined in importance relative to the upper medium car sector, where BL's presence is currently weak, and as a result BL achieved lower than expected shares of the total market. Jaguar has benefited from the strong dollar and from great improvements in perceived quality.

Unipart

2.9 Unipart's performance has been disappointing, the PBIT shortfall arising in the parts sales operations (rather than the manufacturing division) as a result of economic conditions in domestic and overseas markets.

Leyland Group

2.10 In recommending that the 1982 Leyland Group Plan be approved, the Interdepartmental Group was aware of the magnitude of the task facing the Group and the risks attending its achievement. In view of the risks involved, the BL Corporate Staff has inserted central contingencies into the total BL budget against such worse than Plan performance. The latest forecast PBIT of £(37.2)m means the PBIT contingency is overrun by £6.1m; the Group still expects to perform within the cashflow margin allowed by the centre. However, the UK operation, Leyland Vehicles Limited (LVL), where the performance shortfall was expected to occur, is only responsible for just over half of the profit shortfall - the bulk of the rest occurs in the two major overseas operations, Ashok Leyland in India, and Leyland South Africa. Furthermore, following the unsuccesful strike at the start of the year, facility rationalisations have gone ahead with the cooperation of the workforce and the underlying physical progress at LVL has been more encouraging than the financial results would suggest. New models are being progressively introduced, and material and model profitability targets are now being met.

Land Rover

2.11 Economic problems in major African and Middle-Eastern markets have meant that sales volumes have only been maintained at the cost of lower margins. The van manufacturing division, Freight Rover, has recovered from poor 1981 figures and is now approaching breakeven.

Conclusion

12 Against the economic background, 1982 performance for BL as a whole was broadly satisfactory, and supports the prospect of continuing recovery. In the Leyland Group, performance in 1982 leaves a question mark - as there was one at the beginning of the year. But the Group's progress has its encouraging points and its results are by no means so poor, taken in themselves, as to rule out the prospect of recovery.

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III. KEY FEATURES OF THE 1983 PLAN

Overall features

3.1 As in the 1982 Plan, BL as a whole is projected to achieve breakeven at the trading level in 1983 and to approach breakeven after interest and tax in 1984. Within this overall performance, the old Cars Group (now subdivided into ARGH and Jaguar) is still projected to achieve breakeven before interest and tax in 1984. The Unipart and Land Rover Groups are expected to show steadily increasing profits over the Plan period. The Leyland Group is forecast to return to profit at the trading level in 1983 and to achieve a profit after interest and tax in 1984:

FORECAST PROFIT/(LOSS) BEFORE INTEREST AND TAX - £m

	1981	1982	1983	1984	1985	1986	1987
ARGH	(167)	(126)	(64)	(9)	16	41	49
Jaguar	(24)	12	10	19	36	44	58
Unipart	14	11	20	23	28	30	32
Land Rover	17	8	23	39	58	74	76
Leyland	(74)	(29)	21	78	128	135	143
Central Services/ Other Companies/ Consolidation	(11)	(10)	(6)	(9)	(9)	(8)	(6)
Total BL plc	(245)	(134)	4	141	257	316	352

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3.2 Since the Plan was submitted, BL have revised their forecasts of PBIT in 1982 as follows:

1982 PBIT (£m)

	1983 Plan	Forecast	Forecast b/(w) than Plan
ARGH	(126)	(115)	11
Jaguar	12	12	-
Unipart	11	11	-
Land Rover	8	7	(1)
Leyland	(29)	(37)	(8)
Central Services/ Other companies/ Contingencies	(10)	(13)	(3)
Total BL plc	(134)	(135)	(1)

These revised figures are still broadly in line with the financial trends shown in the 1983 Plan.

3.3 Although the broad trend of financial performance on profit and loss account is comparable with that in the 1982 Plan, projected profit before interest and tax over the period 1981-6 is forecast to be £(92)m worse than in the previous Plan, and £(125)m worse over 1983 to 1986. This projected shortfall breaks down as follows:-

PBIT better/(worse) than in the 1982 Plan

	1981	1982	1983	1984	1985	1986	Total 1981-6	Total 1983-86
ARGH	12	10	(18)	(9)	1	(2)	(6)	(28)
Jaguar	-	7	4	-	(1)	3	13	6
Unipart	2	(2)	(5)	(11)	(12)	(19)	(47)	(47)
Land Rover	13	(4)	(9)	-	-	4	4	(5)
Leyland*	6	2	1	(9)	13	(9)	4	(4)
Central Services/ Other companies/ Consolidation+	(11)	(2)	4	(18)	(15)	(18)	(60)	(47)
Total BL plc	22	11	(23)	(47)	(14)	(41)	(92)	(125)

*1983 Plan compared with 1982 Plan after allocation of centrally held contingencies.

+The relatively large negative sums appearing under this heading for the years 1984-6 reflect two main factors:

a) The 1983 Plan, unlike the 1982 Plan, does not consolidate the post-1982 results of Aveling Barford and Goodwin Barsby which should shortly be disposed of. These companies were projected in 1982 to produce a combined PBIT in 1984, 1985 and 1986 of £3m, £7m and £7m respectively.

b) The revised projections for Central Services (chiefly BL Systems) over the three years.

The main shortfall on the 1982 Plan figures (leaving aside Leyland, for which a contingency was deliberately created in the 1982 Plan) occurs for Unipart; other Groups are still projected to perform much as in last year's Plan. The deteriorations that occur are largely accounted for by the fact that the 1983 Plan, when compared with the 1982 Plan, projects lower demand (especially for Unipart), a greater alignment of UK and European car prices and slightly higher sterling exchange rates towards the end of the Plan period. These factors are expected to be largely offset by further significant improvements in cost performance.

3.4. Despite this deterioration in PBIT over the Plan period, projected cash outflow over the period is held broadly in line with that in the 1982 Plan. Since the allocation by BL of debt to the operating companies is somewhat arbitrary the following table gives the operating cashflow (ie net of interest) for each company, and interest charges are shown separately.

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1983 Plan operating cashflow forecasts

£m	1981	1982	1983	1984	1985	1986	1987
ARGH	(235)	(255)	(148)	(73)	(16)	42	2
Jaguar	(43)	(30)	(34)	(12)	26	10	15
Unipart	18	(5)	16	7	12	24	27
Land Rover	4	(36)	(13)	33	46	48	47
Leyland	(61)	(104)	(40)	3	67	54	30
Central services/ other companies +	45	(5)	(2)	(2)	-	1	2
Interest charges	(88)	(100)	(112)	(117)	(122)	(112)	(96)
Consolidation	(41)	11	(25)	(13)	(1)	(7)	(7)
Total BL plc	(401)	(524)	(358)	(174)	12	60	20

+The high cash inflow shown here for 1981 reflects largely the disposal of Prestcold, Alvis and Coventry Climax.

A direct comparison of operating cashflow forecasts with those in the 1982 Plan is not possible because of the re-organisation of the company. However, interest costs in the 1983 Plan are broadly similar to those in the 1982 Plan, and the allocation of debt to the operating companies appears broadly unchanged, so that the differences between the overall cashflow forecasts in the two Plans can largely be attributed to operational factors rather than changes in interest.

1983 Plan cashflow forecasts: better/(worse) than 1982 Plan.

£m	1981	1982	1983	1984	1985	1986	Total 1981-6
ARGH	87	12	(25)	(40)	(19)	1	16
Jaguar	2	2	7	(7)	(1)	(7)	(4)
Unipart	36	(12)	11	(3)	(7)	(4)	21
Land Rover	25	(6)	(20)	3	(1)	(2)	(1)
Leyland	18	17	(24)	(3)	10	(24)	(6)
Central services/ other companies	32	10	13	11	10	10	86
Consolidation	(55)	10	(15)	(24)	(10)	(2)	(96)
Total BL plc	145	33	(53)	(63)	(18)	(28)	16

However, this apparent marginal improvement in cash outflow over the Plan period represents an improvement in 1981-2 totalling £178m and a subsequent deterioration (compared with the 1982 Plan) of £162m in the period 1983-6. The improvement in 1981-2 largely reflects lower than planned capital expenditure (£468m incurred as against £601m planned) and lower than expected losses (actual PBIT £(379)m over the two years as against £(412)m expected). The subsequent deterioration in cashflow reflects the downgrading of earnings forecasts from 1983 onwards, while assets overall are projected to be at about the same level as in the 1982 Plan.

3.5 The regional implications of the Plan are considered at Annex 2. In summary, the only feature of the Plan which might be expected to increase pressure for an upgrading in Assisted Area status is the cessation of assembly at Bathgate in 1984. It is also possible that any significant resourcing of BL components from overseas would increase unemployment in the West Midlands and increase the pressure for Assisted Area status there, but we cannot assess the likelihood of this at present.

3.6 Whether BL's plan can be achieved will depend partly on how far its forecasts of developments in the national and world economy are realised. The official view of the immediate prospect, as set out in the Industry Act forecast, is close to BL's. World activity is expected to be a little lower than BL assume but UK consumer expenditure is expected to be a little higher. BL's assumptions about domestic cost increases look too high in view of current inflation trends. The company's sales and profits should also benefit from the recent drop in the exchange rate, if it proves permanent, which BL's forecasts do not allow for. In the longer term BL have assumed that a rise in the real oil price in 1984 results in a cyclical downturn in the UK and world economies in 1985. This is possible but the official view is that the recovery from the present deep world recession will be more prolonged. Our overall assessment of BL's economic assumptions is therefore that they are slightly pessimistic. We belive this is sensible for planning purposes. There is no risk that BL will forgo market share because they have taken this view; but failure to be cautious could have caused BL to make over-optimistic plans.

Austin Rover Group Holdings

3.7 The product and marketing strategy for ARGH is broadly similar to that in the 1982 Plan, although there have been some changes in timing. The basic strategy remains to achieve a coherent manufacturing and marketing base by the mid-1980s as follows:

Plant	Models and launch dates		Product range
Longbridge	Metro	Oct 1980	small car family
	Acclaim*	Oct 1981 (facelift 1984)	
Cowley	LM10	Spring 1983	medium/ executive. family
	LM11	Spring 1984	
	XX	Spring 1985	
	LM16	Spring 1986	

*currently produced at Cowley

Broadly speaking, the LM10 and LM11 will be directed at the medium sector (competing with such cars as the Ford Escort and Sierra and the Vauxhall Cavalier) while the XX (the Rover replacement) and LM16 (the Ambassador replacement) will be directed at the upper medium/executive sector. There will be a high degree of component commonality between the models in this family, and this, together with the use of flexible manufacturing systems, will enable economies of scale to be achieved. In the longer term, the Plan envisages replacement of the small car family in the late 1980s, with the Acclaim to be replaced in 1989 by the LM5 and the Metro to be replaced in 1990 by the LM6. It is too early to estimate the capital cost of this programme, but BL believe it will be comparable to the LC10 programme, which has involved capital expenditure of some £200m. The Acclaim facelift, as well as the LM5 and the LM6, will be produced at Longbridge, so that by the mid-1980s each family of cars will be produced at a dedicated manufacturing plant (Longbridge for the small car family, Cowley for the medium/ executive family).

3.8 The introduction of this strategy has involved the rationalisation of plant facilities and the phasing out of old models. This process is now virtually complete. During 1982 the company have closed Solihull, Speke No. 1, Coventry Engines and CAB2 at Longbridge, and disposed of Alford and Alder and Rearsby Components. Production of the Allegro ceased early in the year: the next models to be phased out will be the Mini and the Ital in mid-1984, to be followed at end-1984 by the Rover and at end-1985 by the

Ambassador. In the meantime the Ital has been transferred from Cowley to Longbridge, so avoiding redundancies there and freeing labour at Cowley for the LM10.

3.9 An important feature of this product strategy is the extent to which economies of scale are achieved by collaborative ventures. The Acclaim is the first model ARGH have produced in collaboration with Honda, and the Acclaim facelift (which will be significantly different from the existing Acclaim) is also to be a collaborative project - possibly to be carried out by a joint company established by ARGH and Honda expressly for the purpose. The XX is also to be a collaborative project with Honda, and once again there is a possibility that a joint company might be established. If the problems in the European market which have been encountered with the Acclaim are to be avoided, BL and the Government will need to ensure that these ventures are carefully presented to our European partners as being different in kind from, and much more of an equal partnership than, the initial collaboration on the Acclaim.

3.10 The most important phase of this product strategy is the introduction of the LM10 and LM11, which ARGH are expecting to take up to 9% of the market by 1985. For several years ARGH has been represented in the increasingly important medium car sector only by ageing models of limited appeal (eg Allegro, Ital). If the LM10 and LM11 are successful ARGH will be able to break into this sector, with corresponding benefits to their sales volumes and market share, which are projected as follows:

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UK Car sales	1981	1982	1983	1984	1985	1986	1987
Volume (000)	277	259	287	337	347	358	358
Market share	18.7%	17.4%*	18.5%	20.4%	22.4%	22.4%	22.4%
Volume better/ (worse) than 1982 Plan (000)	(5)	(25)	(15)	16	(3)	6	N/A
Market share better/ (worse) than 1982 Plan	(0.4)%	(2.1)%	(2.3)%	(1.0)%	(0.9)%	(1.1)%	N/A

* Since preparation of the Plan ARGH have revised their forecast market share for 1982 to 17.3%.

Although market share is projected to remain consistently below the levels projected in the 1982 Plan forecast volume over the period 1983-6 is very slightly increased, which reflects a rather more optimistic view of economic conditions, and thus of total industry volume (TIV), over the period:

TIV	1981	1982	1983	1984	1985	1986	1987
1983 Plan (000)	1485	1490*	1550	1650	1550	1660	1600
Higher/ (lower) than 1982 Plan (000)	8	35	100	150	50	100	N/A

* The latest forecast TIV for 1982 is 1,549,000 vehicles.

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3.11 The programme of manpower reductions in ARGH is now almost complete, although there are still redundancies to come in 1983. These redundancies will be partly offset by the recruitment now under way at Cowley to man a second shift on the LM10 lines. Productivity over the Plan period is now forecast to rise rather more than in the 1982 Plan:

1983 Plan	1981	1982	1983	1984	1985	1986	1987
Manpower (000)	51	40	36	36	37	37	37
Production (000)	407	381	434	505	525	557	578
Vehicles/ man/year	8.0	9.5	12.1	14.0	14.2	15.1	15.6
1982 Plan (for comparison)							
Manpower (000)	51	45	43	42	42	42	
Production (000)	438	422	458	492	543	552	
Vehicles/ man/year	8.5	9.4	10.7	11.7	12.9	13.1	

This significant improvement in projected productivity levels reflects not only the advanced production facilities now coming into use at Cowley for LM10 production as well as at Longbridge for the Metro but also improved industrial relations and reformed working practices, which should result from agreements between BL and the unions agreed earlier this year. Productivity in October this year was 9.23 cars/man/year, 7% above budget, and now that production of the LM10 has started the above targets look achieveable. (Continental car manufacturers are currently believed to be achieving average productivity levels of about 11 cars/man/year, while productivity at Ford UK is a little over 7 cars/man/year.)

3.12 Capital expenditure in 1982 is forecast in the 1983 Plan to be £109m, although BL have subsequently downgraded this forecast to £101m and there may yet be a further reduction. This compares with a budget figure of £167m (a direct comparison with the 1982 Plan is not possible because that Plan does not separately identify ARGH's capital expenditure). £17m of this shortfall is due to physical savings (eg abandoned or more economical projects), £5m is due to price savings compared with budget, and the remaining £46m is due to the rephasing of expenditure patterns. This rephasing has been achieved without jeopardising the timing of product launch by reducing the lead time of a number of projects. ARGH's capital investment forecasts for future years in the Plan period are as follows:

£m.	1983	1984	1985	1986	1987
	129	152	138	113	197

3.13 ARGH reaffirm in the Plan their determination to keep down component costs, and suggest that if UK component manufacturers cannot compete with foreign suppliers the company may have to resource abroad a significant proportion of its component purchases. The company have however subsequently agreed that before coming to any significant decisions about resourcing they will inform the Department of Industry so that the Department can pursue the possibility of Government assistance (under existing schemes) for investment in the supplying company which would enable it to meet ARGH's requirements on quality, reliability and price. Discussions between ARGH and the Department have already identified some candidates for such assistance.

Risks

3.14 As noted above, the achievement of ARGH's projected market shares - and indeed ARGH's survival in the market place - depend crucially on the success of the LM10 and LM11 - particularly perhaps the LM10, as the first in the range. This model will not be launched until the spring of 1983, and it will not be possible to judge its success in the market until the middle of the year.

3.15 Of the other factors within ARGH's control, perhaps the major threat to achievement of the Plan lies in the risk of prolonged industrial unrest, which would not only damage the company directly but would probably have a lasting effect on its market share. The risk of industrial unrest can never be completely dismissed in the vehicle industry, but a number of signs suggest that there are grounds to hope for a period of peace at ARGH. The agreement on a two-year pay settlement is one such sign; the conclusion of a new industrial relations agreement in June this year is another. Despite all the uncertainties, therefore, it seems reasonable to say that the risk of non-achievement of the Plan due to prolonged industrial unrest is less for this Plan than it has been for previous Plans.

3.16 The other major risks are largely outside ARGH's control; the level of economic activity (and its effect on TIV) and the exchange rate (particularly against other European countries) are perhaps the two most important. These might also be a risk toARGH if UK prices had tobe held down to enable the differential between UK and Continental prices to narrow more rapidly than assumed in the Plan, but recent movements in the exchange rate have already eliminated a large part of the differential. However, as noted above, the economic assumptions underlying ARGH's forecasts are if anything on the cautious side: the recent movements in the exchange rate, for instance, if not reversed should increase ARGH's profits substantially. The risk of non-achievement for these reasons therefore appears reduced.

Conclusions

3.17 ARGH is continuing broadly on the path laid out in previous Plans, although it is too soon to draw any firm conclusions about the long-term future of the company in advance of the launch of the LM10. It is clear, however, that on the results projected ARGH will not be a commercially attractive copany within the Plan period, and that towards the end of the Plan period the question of funding the next model replacement programme will arise. The implications of this are discussed further in Chapter IV, paragraphs 4.17 to 4.19.

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Jaguar Group

3.18 Jaguar is projected to maintain over the Plan period the strong recovery forecast in the 1982 Plan. This strong recovery is based largely on a continuing increase in sales to North America (chiefly the USA) and a determined attempt to break into the West German market (where the luxury car market is over four times the size of the UK equivalent).

Sales volumes (000)

	1981	1982	1983	1984	1985	1986	1987
1983 Plan							
UK	5.7	6.6	6.9	9.0	9.3	9.6	9.6
North America	5.0	9.7	11.5	11.1	12.3	12.2	19.1
Europe	3.0	3.0	4.5	4.5	5.7	6.0	7.0
Rest of World	1.9	2.3	3.0	3.0	3.6	3.9	4.8
Total	15.6	21.6	25.9	27.6	30.9	31.7	40.5
Better/(worse) than 1982 Plan							
UK	(0.3)	(0.4)	(0.1)	-	(0.7)	(1.4)	
North America	-	2.7	3.5	2.1	2.3	2.2	
Europe) Rest of world)	(0.1)	0.3	0.5	(0.5)	(1.7)	(2.1)	
Total	(0.4)	2.6	3.9	1.6	(0.1)	(1.3)	N/A

The sharp increases in sales projected in 1984-5 and in 1987 reflect the introduction in 1984 of the XJ40 (a luxury car replacing the XJ6 and XJ12) and in 1986 of the XJ41 (a sports car replacing the XJS). The launch of the proposed XJ80 (an upper executive 4-door saloon) has been postponed from 1986 to 1988 so as to allow an earlier launch for the XJ41.

3.19 The consolidation of plant facilities foreseen in the 1982 Plan has proceeded in 1982 and will be completed early in 1983. Manpower has declined sharply since 1980, but it is now forecast to increase steadily over the Plan period. The reduction in the workforce in 1982 has been less than that projected in the 1982 Plan, and the increase now projected greater, but productivity is still expected to rise steadily (although the dramatic productivity increases of the past two years will not be repeated):-

	1981	1982	1983	1984	1985	1986	1987
1983 Plan							
Manpower (000) (Av year)	7.9	7.3	7.7	8.1	8.3	8.5	9.1
Productivity (vehicles/man/year)	1.8	3.1	3.4	3.4	3.7	3.7	4.5
Higher/(lower) than 1982 Plan							
Manpower	0.1	0.5	0.5	0.4	0.5	0.6	N/A
Productivity	(0.1)	0.3	0.2	(0.2)	(0.2)	(0.3)	

Conclusions

3.20 The dramatic turn-round of Jaguar has continued, and the company is well on course to achieving its objectives. If anything, the prospects appear somewhat rosier than the Plan suggests. Jaguar's high level of sales to North America means that its profits are dramatically affected by changes in the exchange rate. The 1983 Plan is based on a \$/£ exchange rate averaging a little over \$2/£ over the Plan period, and BL have estimated that a 10% reduction in the exchange rate against all currencies would increase Jaguar's PBIT by £13m in 1983 and £40m in 1987. The most important exchange rates for Jaguar are the \$/£ and DM/£ rates: the latter has not declined in recent months as much as the former. While it is not possible to make precise estimates, it seems fair to say that if sterling continues at current levels, therefore, the profit levels projected in the Plan should be comfortably exceeded.

Unipart Group

3.21 The 1983 Plan projects lower profits than the 1982 Plan; over the period 1982-6, profits are now expected to be £(47)m lower than previously thought. The major part of this shortfall appears to arise in Unipart division, the replacement parts marketing operation, which accounts for almost 80% of the Group's revenue. Sales volumes for this division are now forecast to be substantially lower than in the 1982 Plan, and to decline rather than increase over the Plan period.

Unipart division sales volumes (value - £m - at 1982 prices)

	1982	1983	1984	1985	1986	1987
1983 Plan	300	270	265	260	255	250
1982 Plan	378	403	435	463	487	N/A
1983 Plan better/ (worse) than 1982 Plan	(78)	(133)	(170)	(203)	(232)	N/A

The projected decline in sales over the Plan period reflects the declining BL car parc. Even a projected increase in Unipart's UK "all-makes" sales does not completely offset this; moreover, this increase has to occur in a static UK market, as longer service intervals and greater reliability are expected to counterbalance the slightly larger total car parc. Both BL and all-makes sales projections in the 1983 Plan have been affected by the ban on exclusive sales contracts with dealers arising from the recent MMC report on car parts.

3.22 Because of depressed market conditions, Unipart are assuming annual price increases 3% below the UK inflation rate. To achieve the necessary cost reductions to sustain this, present supply pattern are being reviewed, with the aim of developing fast-moving product lines and withdrawing from slow-moving and unprofitable ones. Fixed costs are to be further reduced. Manpower is to be reduced (from 2,200 at end 1982 to 1,600 by 1987) as a result of the introduction of new systems and automation. Volumes per employee are therefore expected to rise over the Plan period by 6% per annum despite the fall in total volumes.

3.23 The major risk to this plan would seem to be in the assumption of a 15% growth in UK all-makes sales in a static market. Monopolies legislation may also be more damaging than foreseen. The sales organisation is in need of reorganisation and satisfactory retail franchising arrangements have yet to be devised. There is also a risk that the demand for BL model parts, being based on other Group's planned market shares, may be lower than expected. Furthermore, Unipart's third world export markets, rather than recovering as seems to be expected, may remain precarious for some time.

3.24 On the other hand, the projections do not fully reflect the benefits which may derive from the European and USA all-makes business which Unipart hope to develop. Yearly price increases 3% below UK inflation may be unduly pessimistic if demand picks up.

3.25 The manufacturing division, SU Butec, also depends heavily on sales to BL product companies; however, a decline in these is expected to be more than offset by an increase in other sales.

SU Butec: sales volumes (value - £m - 1983 prices)

1983 Plan	Original equipment		After-market		Total	
	1982	1986	1982	1986	1982	1986
BL product cos	39.5	37.5	1.9	1.1	41.4	38.6
Unipart	-	-	17.0	21.3	17.0	21.3
External	5.5	12.4	8.8	13.9	14.3	26.3
TOTAL	45.0	49.9	27.7	36.3	72.7	86.2

SU Butec has already in some areas products and processes while are competitive in world markets, and the introduction of new product and process technology should enable the company to approach Japanese levels of productivity. SU Butec aim to strengthen their volume base by exploiting their technology and expertise through joint ventures and licensing arrangements and by diversifying into non-automotive applications for their technology.

3.26 The major risk to SU Butec's Plan would seem to be the non-achievement of competitiveness targets, which apart from having a general effect on costs and sales, could result in a loss of ARGH's business to overseas competitors. Overall sales growth is assumed in a static market, although not of the order of that sought by Unipart division. However, prudent assumptions are made about the BL market, with Cars and Land Rover volumes taken as 500,000, rather than the 600,000 on which the companies' own plans are based; and sales to these companies are assumed to decline from 57% of all sales in 1982 to 42% in 1987. It may also be possible to reflect cost improvement in higher margins than planned, rather than lower real prices.

Conclusions

3.27 Over Unipart Group as a whole, there hangs the major handicap of a static market resulting from larger service intervals and improved reliability, into which both divisions must make further inroads if they are to achieve their Plan. This depends above all on being price competitive and hence improving the cost effectiveness of manufacturing, storage and distribution systems. Although the risks and opportunities cannot be precisely quantified, SU Butec would seem to have the greatest potential for improvement over Plan, based on its past record of technological development and productivity increases; and this may in some measure offset the risk to the marketing operations.

Land Rover Group

3.28 As in the 1982 Plan the Land Rover Group is projected to made a profit before interest and tax in each year during the Plan period, and to make a profit before tax in every year except 1982. However, although the projected profit level rises steadily from year to year (reaching £76m PBIT in 1987 compared with £8m in 1982), profits in the early years of the Plan are expected to be lower than in the 1982 Plan, and over the period 1982-86 a cumulative shortfall of £(9)m is projected. This deterioration reflects three main factors:-

a) Export sales are now expected to hold up less well than projected in the 1982 Plan, as a result both of the continued recession, which is affecting some of LR's African markets particularly badly, and of intense competition, particularly from Japanese manufacturers.

b) Smaller price increases are assumed than in the 1982 Plan, again reflecting the intense competition in export markets.

c) These effects are partly offset by improvements in cost performance, compared with the 1982 Plan.

3.29 The product strategy for LR is broadly unchanged from that in the 1982 Plan. The main features of the strategy are:

a) the launch in early 1983 of a new model Land Rover, the Stage 2, initially in long (110") wheelbase form and subsequently in a number of variants;

b) the replacement during 1983 of the existing Series III short (88") wheelbase model with the Series IIIa, which will incorporate body changes from the Stage 2 model;

c) a number of improvements during 1983-4 to the Range Rover, with an eye particularly on the North American markets, in which Range Rovers are not currently sold. The decision to attack the North American markets is the major new marketing feature of the 1983 Plan.

In the longer term the Plan identifies the need for a new short-wheelbase model to replace the Series IIIa in the mid-1980s if LR are to stay in the medium-duty 4 x 4 market. LR have not yet decided whether such a vehicle fits in with their overall strategy and, if so, how this model replacement should take place, but they have recently started work on a detailed study of the options which is expected to reach firm conclusions during 1983. One possibility is an all new short wheelbase range aimed primarily at the private sector, and capable of being extended to a longer wheelbase for Range Rover, pick-up and possibly panel van applications. This approach would require substantial resources, well beyond LR's resources, and could only be pursued as a collaborative venture. The alternative would be to adapt the Stage 2 model to shorter wheelbase form: this would however entail a separate programme to modernise the Range Rover.

3.30 Manpower has been reduced over the past two years rather more rapidly than was suggested in the 1982 Plan, and although manpower is expected to rise slightly over the Plan period the rise is less than that predicted in the 1982 Plan:

Manpower (average yr) (000)

	1980	1981	1982	1983	1984	1985	1986	1987
1983 Plan	13.7	11.4	10.7	10.9	11.0	11.0	11.0	11.0
Higher/ (lower) than 1982 Plan	-	(0.7)	(0.4)	(1.0)	(1.0)	(1.3)	(1.4)	N/A

Productivity in 1982 as measured by units per employee has been slightly below Plan levels; it is, however, now forecast to rise rather more rapidly than in the 1982 Plan:

Productivity	1980	1981	1982	1983	1984	1985	1986	1987
Units/ employee, 1983 Plan	4.4	4.6	5.0	5.7	6.3	7.0	7.4	7.5
Better/(worse) than 1982 Plan	-	0.2	(0.2)	0.1	0.5	0.7	0.5	N/A

3.31 Land Rover sales, which in 1982 have been running almost 20% down on the 1980 peak (and below 1982 Plan levels) are projected to increase by nearly 45% over the Plan period, leading to sales projections well below those in the 1982 Plan. Within this overall figure, sales in the UK and Europe are now expected to be better than in the 1982 Plan, with sales in the rest of the world more than offsetting this improvement. By far the greatest part of the increase in sales is expected to occur in the export of KD kits for assembly abroad, usually in African countries. This area of LR's operations has suffered a severe setback over the past year, falling off by a third between 1981 and 1982, but is projected to recover rapidly to last year's level and to increase further thereafter. The rapid recovery in 1983 is in part attributable to orders already obtained, but it is not certain that all the orders placed will in fact lead to exports, because of instability or uncertainty in the ordering countries.

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Land Rover sales (000)

	1981	1982	1983	1984	1985	1986	1987
1983 Plan							
UK	6.9	8.3	9.1	10.6	10.4	10.8	10.8
Europe	6.4	8.4	8.1	9.9	10.7	11.4	11.6
Rest of world - built up	11.0	11.3	11.2	10.7	11.8	12.6	12.6
- KD kits	18.2	12.0	18.5	21.2	22.1	22.7	22.7
TOTAL	42.5	40.0	46.9	52.4	55.0	57.5	57.7
Better/(worse) than 1982 Plan							
UK	0.3	1.4	1.1	1.6	0.4	(0.2)	
Europe	1.8	2.4	1.3	2.4	2.7	2.4	
Rest of world - built up	(0.7)	(2.9)	(4.0)	(5.3)	(6.5)	(8.9)	
- KD kits	(2.4)	(6.7)	(3.5)	(0.8)	(2.2)	(3.1)	
TOTAL	(1.0)	(5.8)	(5.1)	(2.1)	(5.6)	(9.8)	N/A

3.32 Range Rover sales, on the other hand, are projected to increase much more rapidly than in the 1982 Plan, primarily as a result of the decision to attack the North American markets. (Marketing in Canada is due to start in late 1983, and in the USA in late 1984.)

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Range Rover sales (000)

1983 Plan	1981	1982	1983	1984	1985	1986	1987
UK	2.4	2.7	3.0	3.2	3.2	3.2	3.2
Europe	3.7	5.2	5.9	6.3	6.8	7.2	7.5
N America	-	-	0.1	1.4	5.5	6.0	6.5
Rest of world							
- built up	2.9	3.1	3.3	3.8	4.5	4.7	5.1
- KD kits	1.4	1.8	2.0	2.1	2.2	2.2	2.2
TOTAL	10.4	12.8	14.3	16.8	22.2	23.3	24.5

Better/(worse) than 1982 Plan							
UK	0.2	0.5	0.6	0.5	0.2	-	
Europe	(0.1)	1.0	1.4	1.0	0.8	0.8	
N America	-	-	0.1	1.4	5.5	6.0	
Rest of world							
- built up	(0.1)	(0.3)	(0.4)	(0.2)	0.3	-	
- KD kits	0.2	(0.4)	(0.4)	(0.4)	(0.6)	(1.0)	
TOTAL	0.2	0.8	1.3	2.3	6.2	5.8	N/A

3.33 Freight Rover (light commercial vehicle) sales are projected to be about the same overall as in the 1982 Plan. Following the successful launch of the Sherpa van this year the company intends to launch a heavier vehicle, the MT210, in 1984 which will give them complete coverage of the light commercial vehicle sector. Last year's decision to withdraw from exports (which have been of declining importance in recent years) and concentrate on the domestic market is confirmed.

Freight Rover Sales (000)

1983 Plan	1981	1982	1983	1984	1985	1986	1987
Domestic	8.0	10.4	12.6	17.3	18.3	19.7	20.3
Export	3.0	1.9	0.8	-	-	-	-
TOTAL	11.0	12.3	13.4	17.3	18.3	19.7	20.3
Better/(worse) than 1982 Plan							
Domestic	(0.3)	0.7	-	-	(1.2)	0.2	
Export	0.4	1.2	0.8	-	-	-	
TOTAL	0.1	1.9	0.8	-	(1.2)	0.2	N/A

Risks

3.34 The major risk appears to lie in LR's continued dependence on exports of both built-up units and KD kits to developing countries. Many of LR's traditional markets, particularly in Africa, have found themselves in severe economic difficulty in recent years, and there must be considerable doubt about whether they can recover on the timescale postulated by LR, even assuming that the world as a whole pulls out of recession fairly soon. LR acknowledge the economic difficulties in their traditional markets and the effect of the world recession but still predict market growth to average 6.7% over the Plan period. We are concerned that this may be an over-estimate. Moreover, there has been fierce competition, especially in slightly richer markets, which has been exerting a downward pressure on prices which is unlikely to be relieved in the near future. It may well be true, as LR argue, that many of LR's competitors (particularly the Japanese) offer a less sophisticated and robust product, but it is equally true that such a product will suffice for an increasing number of customers.

3.35 A second risk lies in the projected North American launch for Range Rover. There is no reason at present to suppose that this launch will not be successful, but if it is not the prospects for this side of the business would be distinctly less attractive.

3.36 In the longer term, there may be room for concern at the prospect of a gap appearing in the product range in the mid 1980s. LR have however seen this risk themselves, and are devoting considerable attention to resolving the issues quickly. With the advent of CAD/CAM and other advanced engineering techniques the time required to develop a vehicle from concept to production has been sharply reduced in recent years, and so long as LR resolve the outstanding questions in the course of the next year there is no reason to suppose that the model replacement programme (if it is decided to embark on one) will be delayed. We would expect to see in next year's Plan more fully worked ideas in this area.

Conclusions

3.37 The environment in which LR operate has not improved since last year, and may well have deteriorated. Economic difficulties abound in LR's traditional markets, and competition is intense. There are clearly risks to the achievement of the Plan. We are not convinced that sufficient management attention has in the past been paid to addressing the risks identified above, but there are now signs of the increased effort in this area which we believe to be necessary if the Plan is to be achieved. One example of this effort is the increased attention now being paid to the model replacement problem referred to in the previous paragraph. This increased management effort gives reasonable grounds for expecting that the company will be able to build on its well-established reputation and its good products and remain one of the more profitable parts of BL.

Leyland Group

3.38 The 1982 Plan for Leyland Group represented a radical realignment of the facilities, manpower and manufacturing methods of Leyland Trucks, the Group's truck manufacturing arm. This followed a sharp decline in the truck market in the second half of 1980 for which the then management had been unprepared. The 1982 Plan was the first full Plan to be presented by a new management team led by Mr David Andrews, although they had previously prepared a Plan in the summer of 1981 which had been approved by the Board and the Government only as an interim operating base for the remainder of 1981. The 1982 Plan was considerably more cautious in its projections of the market and of Leyland's performance than earlier Plans had been; BL Corporate Staff, however, felt more cautious still and the 1982 Plan contained centrally held contingencies against non-achievement of the Plan objectives. As will be seen from the following paragraphs, events this year seem to have vindicated this judgment.

3.39 The 1983 Plan broadly reaffirms the strategy outlined in the 1982 Plan, although it is based on more cautious assumptions about worldwide sales volumes and the sustainable level of price increases than that Plan. (This downgrading of assumptions means that there is now a coincidence of view between Group management and BL Corporate Staff about the prospects for the Group; there is therefore no need this year to include a centrally-held contingency against non-achievement.) The Leyland Group as a whole is still projected to return to profit at the trading level in 1983 and to produce a profit before tax in 1984:

PBIT (£m)	1981	1982	1983	1984	1985	1986	1987
1983 Plan	(74)	(29)*	21	78	128	135	143
Better/ (worse) than 1982 Plan before contingency	1	(38)	(37)	(56)	(35)	(54)	N/A
Better/ (worse) than 1982 Plan after contingency	6	2	1	(9)	13	(9)	N/A

*Since preparation of the Plan BL have revised downwards the forecast PBIT for 1982 to a loss of £(37.2)m.

3.40 The Leyland Group includes not only Leyland Vehicles Ltd (comprising Leyland Trucks, Leyland Bus and Leyland Parts) but also a number of overseas companies, including Ashok Leyland (India) and Leyland South Africa. Although the contingency in the 1982 Plan was provided against non-achievement of targets by LVL (and especially Leyland Trucks) a large part of the shortfall against Plan can be attributed to these two overseas companies. LVL's projected results in the 1983 Plan are actually somewhat closer to those in the 1982 Plan than the above table suggests, although a direct numerical comparison is not possible. For LVL alone, the 1983 Plan projects PBIT as follows:

£m	1981	1982	1983	1984	1985	1986	1987
	(88)	(61)*	(12)	28	57	39	58

*Since preparation of the Plan BL have revised upwards the forecast PBIT for 1982 to a loss of £(53.5)m.

3.41 The 1983 Plan reflects a number of different assumptions, both about the performance of the market and LVL's performance relative to it, from the 1982 Plan:

	1981	1982	1983	1984	1985	1986	1987
UK Trucks TIV (000)							
1983 Plan	45	50*	57	70	65	60	60
Higher/(lower) than 1982 Plan	(1)	10	4.5	5	(5)	(5)	N/A

*Latest forecast TIV for 1982 is 45,300

	1981	1982	1983	1984	1985	1986	1987
UK Market Share %							
1983 Plan	16.0	14.4*	14.9	16.7	21.2	21.5	21.6
Better/(worse) than 1982 Plan	(0.4)	(1.4)	(0.9)	(2.6)	0.1	(0.1)	N/A

*Latest forecast market share for 1982 is 13.3%

The substantial increase in market share which is forecast to take place over the period 1983-85 reflects mainly the introduction in 1984 of a new range of light trucks, the MT211. Leyland are also expecting markedly to improve their market share in the medium truck sector following the introduction this year of the MT207 range. Leyland have for some years performed badly in these large sectors of the market - which together constitute over 50% of TIV - as as result of their excessive dependence on outdated models and their temporary withdrawal from the supply of small lorries.

LVL Sales Volume
(000)

	1981	1982	1983	1984	1985	1986	1987
1983 Plan	46	49	55	58	60	66	71
Better/(worse) than 1982 Plan.	(5)	(3)	(3)	(13)	(16)	(16)	N/A

3.42 Within LVL there are once again no major changes proposed for Leyland Bus and Leyland Parts (the proposed rationalisation of Leyland Bus facilities is however more likely to proceed as planned following the acquisition by LVL of the 50% shareholding in Bus Manufacturers (Holdings) Ltd previously held by the NBC, which had previously prevented closure of the Bristol plant.) The rest of this section of the report concentrates on Leyland Trucks, which has been at the root of the Leyland Group's UK problems in recent years.

3.43 The main feature of the 1982 Plan was a major cost-cutting programme. One element of this was a rationalisation of truck production facilities, and this has been continued during 1982. The factory at Guy, Wolverhampton has closed during the year, and tractor manufacture has ceased at Bathgate. The long term objective remains to reduce the scale of operations and to concentrate on three dedicated plants: Leyland (for assembly and KD), Bathgate (for engines) and Albion (for axles). Gearbox and cab production is to cease. The continuation of engine manufacture will only be possible through collaborative ventures, and Leyland have already reached agreement with Cummins on the manufacture of the Family I engine (the lightest truck engine) from 1986. Negotiations on the possible collaborative manufacture of a Family III engine, also from 1986, are proceeding with DAF. The remaining two families of engines, Families II and IV, will probably be outsourced - although it is possible that Family III engines will supplant Family IV in all but the heaviest applications.

3.44 A further important element in the cost-cutting programme was a substantial reduction in the workforce and increases in productivity. The 1983 Plan continues this theme: the main difference is that after a slight increase in 1983 manpower is projected to decline even more than in the 1982 Plan.

Employment at end-year (000)	1981	1982	1983	1984	1985	1986	1987
1983 Plan	17.1	10.3	10.8	10.0	9.2	9.0	8.9
More/(less) than 1982 Plan	-	(0.1)	0.4	(0.4)	(1.2)	(1.4)	N/A

Productivity is still expected to increase markedly over the period. Labour productivity, as measured by standard hours per employee, is forecast to increase by over 20% over the next two years:

Productivity

	1981	1982	1983	1984	1985	1986	1987
Standard hours employees, 1983 Plan	380	469	500	569*	564	523	526

* The decline in output per man after 1984 reflects the reduction in engine production where output per man is higher than in vehicle assembly. Productivity in each area of production is still expected to improve throughout the Plan period.

This is clearly a substantial task. However, the company has made great advances in productivity this year, and we have no reason to believe that this trend will not be continued.

Risks

3.45 Although the forecasts underlying the 1982 Plan for Leyland Trucks have been revised downwards in a number of important respects in the 1983 Plan, there remains a substantial risk that targets will not be achieved and that a return to profitability will be postponed. Among the forecasts most at risk are:

a) Market share Leyland's market share is forecast to increase by over 40% in just two years (1983-5), from 14.9% to 21.2%. This increase is crucially dependent on the success of the new truck models referred to above. The latest forecast for market share in 1982 is 13.3%, well below the planned level of 15.8%, and a substantial improvement on current performance will be needed to achieve the Plan figure for 1983.

b) TIV Although revising downwards the TIV forecasts for later years, the 1983 Plan is forecasting a TIV of 70,000 vehicles in 1984, 55% above the latest forecast 1982 figure but still below the level attained in 1979.

c) Price The 1983 Plan is based on the following average price increases:

	1982	1983	1984	1985	1986	1987
1983 Plan	4.0%	10.6%	11.3%	7.0%	5.1%	9.0%
Higher/(lower) than 1983 Plan	(4.0)%	0.4%	3.7%	(2.4)%	(3.5)%	N/A

Although these price increases lead to absolute prices no higher, and in all years but one lower, than those in the 1982 Plan, there must be some doubt whether in the present depressed state of the truck market price increases of this order - especially the relatively high increases postulated for 1983 and 1984 - are realistic.

d) Exports About half of Leyland's export sales are to Africa, and many major customers there have faced extreme economic difficulties in recent years. Exports will also be vulnerable to exchange rate changes. There must therefore be some doubt whether the volume of exports predicted by Leyland (an increase of 70% over the period 1982-86) can be sustained. In particular, exports to Nigeria are predicted to treble from 1982 to 1987, a projection which is crucially dependent on the oil price.

3.46 There is also the danger that the prospects for recovery could be damaged by further industrial relations problems. Following a 4 - week strike at Bathgate earlier this year the workforce seem to have accepted the first, and perhaps the most painful, stage of the manpower-cutting programme on which the company is engaged. It is too soon to tell whether this strike has had a lasting effect on the company's market share. But there are still about 1400 jobs to go, nearly 1000 of them at Bathgate (out of a total of 2134 currently employed there, and employment in 1981 of some 3600), and the prospect of further strikes cannot be ruled out.

Conclusions

3.47 The 1982 Plan for Leyland Trucks was admitted to be subject to substantial risks. Its projections in several important areas, notably profitability, market share and productivity, have been missed. There is a major task ahead, including making up the ground that has been lost against Plan this year. Experience so far does not suggest that the risks are any less than they were last year although they cannot be said to be any greater. Some economic indicators, notably the exchange rate, have moved in Leyland's favour although the intense competition from other manufacturers shows no sign of abating. The prospect of viability remains more or less the same as it was last year. Leyland Trucks recovery is crucially dependent on how the market receives its new model ranges, the MT 207 (launched this autumn) and the MT 211 (due to be launched in 1984).

We shall need to continue to monitor performance very closely and the "benchmarks" system will help us to pick up any adverse developments at an early stage. Meanwhile, the performance of the Group as a whole has been affected by problems in other parts of the Group, although those problems do not appear to call for action as drastic as was required in the case of Leyland Trucks.

IV THE PRIVATISATION STRATEGY

Introduction

4.1 The strategy for the return of BL to private ownership is set out in the Foreword and Section 3 of the main volume of the Corporate Plan. The purpose of this chapter is to describe the strategy and the background to it, to discuss the prospects for privatisation of each of the main businesses, and to consider whether the strategy fulfils the commitment to make early and visible progress on this front which was given in Sir Michael Edwardes's letter of 4 August 1982 to the Secretary of State for Industry and accepted by the Government.

4.2 The key passages in Sir Michael's letter were:

i)"With regard to privatisation, I confirm it is the Board's objective to return BL in whole, and probably by instalments, to the private sector as soon as practicable. We acknowledge the wish of the Government to show early and visible progress to this end, consistent with maintaining the recovery strategy in the Corporate Plan.

ii)"The Board commits itself firmly to the following specific objectives ..... :-

a) To limit BL's requirements for Government funding to the [£990m of equity funding already committed and such part of the £150m of equity funding envisaged in previous Plans for the period after March 1983 as is not offset by estimated proceeds from the sale of minority interests and which can be demonstrated to be needed to fulfil the Plan]. This will mean that the final £150m funding requirement should be significantly reduced".

b) "To devise a strategy for full privatisation in the 1983 Corporate Plan which offers visible progress within the next two years towards privatisation by such means as the sale of minority equity stakes in BL's more profitable businesses; which builds on existing collaborative arrangements (such as Austin Rover/Honda) and seeks new opportunities for collaboration ...... in order to make BL's constituent businesses more attractive for ultimate privatisation; and which maps out possible routes for the full return of all parts of BL to private ownership by the late 1980s, setting target dates wherever possible".

4.3 In the two months after the despatch of Sir Michael's letter, and in the light of the agreement reached with the Government, BL prepared the fairly detailed privatisation strategy included in the 1983 Plan. They also kept in mind the first of the strategic objectives recently agreed with the Government*, on which the Plan is based, namely "to return all the constituent businesses, either together or separately, to the private sector as soon as practical; if the return of a constituent business carries the risk of reduced viability of the remainder, the issue should be put to the Secretary of State with options".

4.4 In the course of October, the BL Board decided, after receiving advice from their merchant bankers, Hill Samuel, that the act of privatising the profitable and cash generating sections of the business would have a severe impact on the ability to fund the remainder. With the companies added together and regarded as one entity, the Plan would meet the commitment that BL would not need further operational funding by the Government after 1984. However, if the profitable parts were sold, the residual business would require further operational funding because of heavy requirements for capital expenditure on new models just beyond the Plan period.

4.5 At a meeting with the Secretary of State towards the end of October, the Board said that on certain assumptions about the sterling exchange rate, market volumes, car prices and other factors, the Austin Rover business could be left with a requirement for external equity capital after the financial year 1983-84 if

* See the Chancellor's letter of 5 August 1982 to the Secretary of State for Industry (copied to E(NI)).

privatisation of Unipart and Jaguar went ahead. There were a number of ways in which this situation could be reconciled with the undertakings in Sir Michael Edwardes's letter of 4 August. Much would depend on the timing of privatisation of Unipart and Jaguar and on the out-turn of economic factors of the kind mentioned above. The development of the collaboration between BL Cars and Honda, which might lead to Honda taking a minority equity stake in Austin Rover, would be particularly crucial.

4.6 The Secretary of State held the Board to the commitments in the letter of 4 August. He reminded them that Sir Michael had given an undertaking both that no further Government funds would be required for maintenance of the business after the financial year 1983-84 and that there would be visible progress within the next two years towards privatisation by such means as the sale of minority equity stakes in BL's more profitable businesses. He said that he regarded both parts of this undertaking as remaining valid, but he had no wish to press the Board to reach a premature decision about how the objectives would be achieved. The BL Board accepted Mr Jenkin's point of view, and they have set out in the Foreword of the Plan the options for Austin Rover which they will examine to enable BL to meet the objective of privatisation while avoiding the need to call on the Government for further operational funding.

BL's Privatisation Strategy

4.7 The problem presented by Austin Rover will be discussed later in this chapter. A summary now follows of BL's strategy for privatising its other main businesses.

a) Unipart Group

The Unipart Group position is still being worked through. For privatisation, the vehicle companies (Land Rover, Jaguar and Austin Rover) must have adequate control over their service parts operations. At present, Unipart Group provides this service under terms which are satisfactory while the vehicle companies and Unipart are part of BL, but not if they are privatised and so owned separately. Discussions on revised, commercially "arms-length" contracts are being held with the vehicle companies, and the aim is to make a decision by the end of 1982 as to whether such contracts are feasible or not. If contracts can be agreed and drawn up during 1983, then Unipart Group will be a strong candidate for privatisation. 1984 would be the earliest possible date, but BL do not yet know whether this could be achieved. As a step towards privatisation, negotiations are in progress between BL and Burmah Oil about the possibility of forming a joint company between Unipart Group and Quinton Hazell, a components company owned by Burmah.

b) <u>Jaguar</u>

On the basis of the Corporate Plan projections for profitability and cashflow, BL and Hill Samuel agree that it would be possible to sell Jaguar in toto in 1984. However, this would involve an asset write-off of £105 million and earnings of £110 million would be lost in later years of the Plan, so the BL Board would be under an obligation to consider the position of the minority shareholders. Their assessment is that selling Jaguar in 1985 would give higher proceeds and little or no write-off.

The main factor affecting the method of privatisation is a judgment on whether Jaguar can stand completely alone or not. In BL's view, Jaguar needs access to both technical and financial support during periods of product renewal and financial support during weak business periods. Technical support could be provided by strong collaborative ties with another vehicle manufacturer, and for this BMW appears to be the main candidate. Much will depend on the way the current negotiations between the two companies develop. For financial strength, investors with access to substantial sums of cash are needed, and this points to disposing of a substantial stake in Jaguar to a single investment entity.

c) Land Rover and Leyland Groups

BL's preferred strategy is to privatise the two Groups as one entity, Land Rover - Leyland Ltd. However, this depends on Leyland Vehicles' recovery. The events of 1983 will give a clearer picture of what will be possible and, because of poor financial results, no privatisation could take place until 1984 at the earliest. If, towards the end of 1983, it becomes clear that the preferred strategy is not practical within a reasonable timescale, steps will be taken to sell a minority stake in Land Rover UK Ltd.

Accordingly, the following strategy is proposed by BL:

i) For 1983, keep Leyland Vehicles Ltd and Land Rover UK Ltd as substantially separate management and legal entities under the ownership of Land Rover-Leyland Ltd.

ii) Establish now the legal and administrative structure needed to privatise the two Groups as one entity.

iii) If Leyland Vehicles' recovery and Land Rover's progress are as planned in the second half of 1983, develop action plans for the privatisation of Land Rover-Leyland Ltd, either in whole or in part, as early as possible. If the planned results for 1983 are fully achieved, this could conceivably be in 1984. However, in order to give time for a reasonable "track record" to be established, 1985 or later is more likely.

iv) If events in 1983, even if they do not dictate that Leyland Vehicles should be closed, show that combined privatisation is likely to be significantly delayed, consider selling a stake in Land Rover UK in 1984. BL do not yet know at what precise stage next year their Board will be taking a view on this.

v) If Leyland Vehicles Ltd does not recover and is declared beyond reach, and the bulk of the business has to be closed, then plan to sell Land Rover UK Ltd and the overseas companies in the Group and liquidate the residual Leyland Vehicles assets.

The Prospects for Early and Visible Progress

4.8 It is accepted by BL that the two years within which the Government expect to see visible progress towards privatisation date from Sir Michael Edwardes's letter of 4 August to the Secretary of State; and that visible progress entails that by August 1984 some of BL's constituent businesses will have been privatised (either in whole or in part) or a public announcement will have been made of their imminent privatisation, either in whole or in part. BL realise that the Government would obviously prefer a sale to an announcement.

They have agreed that the constituent businesses for this purpose comprise Austin Rover, Jaguar, Unipart, Land Rover, and Leyland Group, and that visible progress has to be made in privatising at least two of these businesses. They have also agreed that to meet their commitment to reduce significantly the final £150m of Government funding envisaged in previous Corporate Plans, they should aim to cut this figure by around £50m. BL will try to fund this portion of the final £150m out of the proceeds of privatisation. However, as no proceeds are expected before 1984 at the earliest, they have assumed in the Plan an increase in borrowing for 1983-84 to offset the £50 million reduction in Government equity in that financial year.

4.9 Taking the businesses in the same order as before, our assessment is that there is a reasonable chance of at least partial privatisation of Unipart within two years. If a joint company can be formed between Unipart Group and Quinton Hazell this would strengthen the Unipart "all makes" and SU Butec operations (those parts of Unipart Group which are not entirely dependent on Austin Rover, Jaguar and Land Rover). However, much remains to be done before a practical proposal can be made. In particular, a firm position on the service parts contracts with these three companies will not be reached until the end of this year. So far, discussions with Austin Rover and Jaguar are at an advanced stage, but the contracts would only be for a duration of three to five years, which would be likely to affect adversely the valuation of the Unipart business. The Quinton Hazell position will not be finalised until early in 1983.

proposal (conveyed to the Department informally) is that the merged company formed from Quinton Hazell and Unipart should have a BL majority and a private sector minority - possibly Burmah Oil themselves initially, who would then sell out to minority holders (probably financial institutions). We understand that the BL Board have discussed this in general terms, and have agreed that Mr Ray Horrocks should contact Burmah and Quinton Hazell for the further information which would be needed before a final decision could be taken. This proposition apart, the projections for the Unipart Group's profits and cash flow included in the 1983 Plan are less good than those in the 1982 Plan, but, if achieved, they would still be sufficiently good to justify BL's hopes of privatisation 1984 or 1985.

4.10 Jaguar is clearly regarded by BL as the front-runner in the privatisation stakes. It is the only business for which BL have so far obtained an up to date valuation from Hill Samuel. There has been a remarkable recovery in the business in the past year, and the financial projections included for Jaguar in the 1983 Plan show that there are good prospects of meeting the objective of privatisation (either partial or total) in 1984 or at least making an announcement in 1984 of privatisation in 1985. However, the Board point out that selling Jaguar in 1984 would involve a write-off of around £105m in the value of the assets and also a loss of about £110m in the earnings which Jaguar would otherwise bring to BL in later years of the Plan. The Board say that they would be under an obligation to consider the position of the minority shareholders in these circumstances, as selling in 1985 would give higher proceeds and little or no write-off. We have asked BL for a note on their point about the position of minority shareholders so that we can assess, in the light of legal advice, whether there is any substance in it. It is the sort of point in which, given the duty of Boards of Companies Act companies to have regard to the interests of all their shareholders, the Public Accounts Committee could be expected to take an interest. However, at first sight it could probably be argued convincingly that the only reason why the shares in BL held by the minority shareholders have any residual value at all by now is the huge investment which the Government have made in the company.

4.11 From a financial point of view, it would be better for BL as a whole if Jaguar were not privatised until 1985. From Jaguar's point of view, it might not be beneficial to remain with the rest of the BL Group for too long. However, even from Jaguar's point of view, there are arguments for privatisation taking place in 1985 rather than 1984. The new XJ40 model is being launched in 1984, and if privatisation took place in that year it would not be known beforehand whether the new model was a success. Moreover, if any technical problems became apparent soon after the launch, it would be easier for Jaguar to obtain help from BL Technology if they were both still part of BL. In the light of these considerations, it would be best to leave the initiative with the BL Board to make proposals to the Government about the best timing for the privatisation for Jaguar as long as they keep to the commitment which they have made to the

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Government on early progress toward privatisation. It would be open to the Government, when they received BL's proposals in relation to Jaguar, to seek independent advice on such matters as the timing and likely proceeds of the disposal.

4.12 As to the method of privatisation, we would not dispute BL's view that Jaguar needs access to both technical and financial support during weak business periods. Negotiations have been in progess for some time between BL and BMW about possible collaboration in such fields as production of a new joint model and joint marketing in certain areas. We understand from Mr Horrocks that there has been some delay since the last round of discussions between the two companies. He thinks it possible that BMW have been holding back in order to see what the Government's views would be on the question of BMW eventually gaining control of Jaguar. Following consultation of DoI Ministers, Dr von Kuhnheim (Chairman of BMW) has been told:

a) that the Government would be unlikely to favour outright sale of Jaguar to a foreign company, or any arrangement under which eventual control went outside the UK;

b) provided it arose in the context of a commercial collaboration negotiated with BL, the Government would be content with an arrangement under which BMW took a minority stake in Jaguar, or established a joint company or companies to pursue particular pieces of collaboration, or indeed if there were collaboration without the setting up of a joint company.

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4.13 Dr Von Kuhnheim's reaction was that foreign control over Jaguar would destroy the company, and for that reason BMW would not seek to gain control. However, he was quite open to the possibility of collaboration between the two companies on a number of fronts. The prospects for this should be clearer when they next meet.

4.14 The BL Board are doubtful about Jaguar's ability to stand entirely alone. Given that collaboration with BMW might provide the necessary support on the engineering side, Hill Samuel have been asked to consider the financial aspects of independence. Kleinworts have already advised that, in principle, institutional funds could be found to buy Jaguar. It would seem that BL are, in general, proceeding in a sensible manner with regard to the privatisation of Jaguar.

Land Rover - Leyland

4.15 We are inclined to the view that BL's preferred vehicle for privatisation of these businesses - a combined Land Rover - Leyland Ltd - would be too large to interest a single potential purchase in 1984 or 1985 (as the company envisage), though it might be of some interest to financial institutions. The projections of profit and cashflow look satisfactory for 1984 and even better for 1985 onwards, but there must be serious doubt about whether such good results will be achieved. The Board themselves acknowledge this in relation to the Leyland Group. In view of this, we doubt the wisdom of creating now a single legal entity to bind the two operations more closely together. This might create extra problems later on if the two need to be privatised separately. We also have the impression that BL may be overplaying the synergies between Land Rover and Leyland. The Secretary of State for Industry has already urged the BL Board to consider whether it would be possible to attract interest from the financial institutions in a partial flotation of the combined Land Rover - Leyland business in 1984 or early 1985, and has offered to facilitate discussions betwen BL and the Bank fo England to this end.

4.16 BL envisage that, if towards the end of 1983 it becomes clear that their preferred strategy is not practical within a reasonable timescale, steps should be taken to sell a minority stake in Land Rover UK Ltd as soon as possible - probably in 1984. In our view, if Ministers decide to approve the 1983 Plan, it would be as well to say to BL in the letter conveying approval that Ministers want this option to be kept fully open, and for this reason they would prefer the Board not to proceed now with any measure, such as creating a single legal entity to bind the Land Rover and Leyland operations more closely together (unless this were no more than a holding company), which would make privatisation of Land Rover on its own more difficult to achieve.

Austin Rover

4.17 As mentioned in paragraph 4.5 above, one of the main issues identified in the 1983 Plan is the poor results projected for the Austin Rover business and the need for further action to be taken to resolve the issue. In previous Plans the problem has been to some extent masked because projections have been given for BL Cars as a whole. However, the Plan contains little that is new on the subject of Austin Rover, although some of the issues are spelled out in more detail by BL than has been the case previously. BL have always argued, and the Government have at least recognised the argument, that Jaguar or Land Rover should not be sold off separately but should be retained with volume cars as one entity to be sold off in one block. The argument rested on the premise that over the next five years or so the volume cars side of the business would not be attractive to prospective purchasers, but that with the inducement of Land Rover and/or Jaguar, the likelihood of disposing of volume cars (as part of a package) would be enhanced - even if some dowry might still be required. This is still very much the argument of Option 2 for Austin Rover in the Foreword to the Plan.

4.18 The slightly new departure is Option 1, where BL intend to explore the possibility of improving Austin Rover's performance still further in order to raise its financial results in the coming years to commercially acceptable levels. The outlook - at least on the five year timescale we are considering - does not look promising; but in previous recent plans it has been taken more less as fact that the volume cars side of the business could not be transformed in this period into a separate saleable entity. It has also been recognised that even in the longer term, BL could not be viable as a fully integrated and independent volume car producer. Collaboration has been seen as a way of helping to overcome this problem. In this Plan, the proposed collaboration with Honda is identified as an important opportunity. The possibility exists of forming a joint company with Honda to manufacture the Triumph Acclaim "facelift" for both companies and this approach could well be extended later to embrace the new XX executive model. This link with Honda would strengthen Austin Rover in many ways, by providing some capital equipment at little or no cost, by helping to improve operating efficiency, and providing the vitally needed increase in production volumes. It would also make it more attractive to private investors. News of whether the joint company approach is likely to proceed is expected at the end of January 1983.

4.19 We have considered whether, as BL propose, the options relating to Austin Rover can await evaluation in the 1984 Corporate Plan. Our conclusion is that they can, because the measures of privatisation (of Jaguar and Unipart) that would trigger the problem will not take place until 1984 at the earliest. Moreover, there is also the need to see whether the LM10 is a success and whether further collaboration with Honda is likely to proceed. We understand that Mr Ray Horrocks has in mind a review of the Austin Rover business next year some months earlier than would be necessary for the 1984 Plan. Clearly, the Government will need to be informed of the results of this exercise.

Restoration of BL's Balance Sheet

4.20 Sir Michael Edwardes's letter of 4 August contained a paragraph spelling out the only circumstances in which (besides the triggering of the Varley/Marshall/Joseph assurances to creditors in the event of collapse of the business) Government funds might be needed after the cessation of operational equity funding in 1984. The paragraph runs as follows:

> "We have an unacceptable balance sheet for privat sector purposes, and as we privatise we will need to remedy the position for those companies taking on outside shareholders or joining the private sector. There might be a need for Government finance immediately prior to privatisation, but the aim would be at least to recover any outlay by the proceeds of disposal."

4.21 In the past few months BL have prepared a strategy for privatisation and not a detailed plan of implementation. They consider that there is a strong likelihood of further financing requirements both during the period it continues as parent of the operating companies and after all its subsidiaries have been sold. As an illustration of the implications of a sale during the privatisatiion process, some preliminary calculations have been made on the assumption that all the equity of Jaguar is sold for £70m at the end of 1984. In that instance, the funding implications might be as follows over the period 1985 to 1987 (the last year covered by the Plan).

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ILLUSTRATION: FUNDING IMPLICATIONS OF SALE OF JAGUAR

	£
Proceeds from sale	+70
Loss of Plan operational cash flow in 1985-1987, before financing	-51
	+19
Financing costs of borrowing no longer assumed by Jaguar (say £100m for 3 years)	-30
Increase in funding requirement 1985-1987	-11

In addition to the above incremental funding requirement of £11m, a major asset sale could have an unfavourable effect on the overall borrowing capacity of BL, implying greater exposure for Goverment. On the assumption that privatisation is completed by the end of 1987, BL have estimated the liabilities which the Government will face under the Varley/Marshall/Joseph assurances. These liabilities arise because it is not considered that BL could, on being privatised, support Plan levels of borrowings and such borrowings would therefore need to be refinanced. By the end of 1987 BL group borrowings are forecast at £1,018m. BL consider that the proceeds of sales of subsidiaries would fail to meet BL's liabilities under these borrowings. Their more favourable calculation of the remaining liability reveals a further funding requirement of £120m; their less favourable calculation shows a further funding requirement of £500m.

4.22 It is, of course, possible (as BL say) that the sale proceeds could be higher than assumed in BL's more favourable case, especially in the case of Land-Rover-Leyland if the Corporate Plan earnings forecasts are achieved and believed by the market to be sustainable.

On the other hand, the range of Government funding mentioned by BL may equally well be understating the size of the problem, especially if Austin Rover (where the bulk of the problem lies) had to be sold for less than, say, the 15 per cent of its asset value which was assumed in their less favourable assumption on disposal values.

4.23 In considering this question, the following factors should be borne in mind. Whatever the prospects for the Austin Rover business (whether there is a partial or total collapse, whether it performs in accordance with Plan, or whether it performs better or worse than Plan) the Government are committed by the Varley/Marshall/Joseph assurances to meeting BL's debts until full privatisation is complete (though the company have promised to explore the practicality of reducing the scope of the assurances as privatisation proceeds). Given this fact, it will be for the Government to decide, and the timing will be at their option, whether, and if so when to liquidate any rump of BL which cannot be sold by the late 1980s. If the current Austin Rover forecasts are achieved, any continuing funding requirement at that time should be able to be met by borrowing rather than the provision of equity capital, albeit backed by some form of Government assurance. If such borrowing had to be backed by a Government guarantee, it would be akin in resource terms to the provision of equity capital. However, Austin Rover are likely by then to be generating sufficient profits to service and repay their loans. Over a new model cycle taken as whole, they would be generating enough cash to satisfy their needs. However, like most other companies, they would need loans for cashflow reasons to finance capital investment at a particular stage in the model cycle.

Conclusion

4.24 The conclusion of this chapter is that there are reasonable prospects for visible progress towards the privatisation of Jaguar and Unipart in the next two years. A strategy has been produced for privatising the Land Rover and Leyland Groups together by 1985, but we have reservations about whether this is the best strategy available. The prospects for privatising Austin Rover are very poor, but BL have action in hand to deal with this problem in the course of next year without calling for further Government funds. Overall, our judgment is that the privatisation strategy which BL have prepared for the 1983 Plan fulfils the commitment given in Sir Michael Edwardes' letter of 4 August 1982. However, details of how the strategy should be implemented have not yet been worked out by BL, and it will be necessary for the Department of Industry to monitor progress on this in the course of next year.

V. SUMMARY OF CONCLUSIONS AND RECOMMENDATION

5.1 We conclude that BL as a whole is still on the course towards viability which has been plotted in previous years' Plans, although the prospect of eventual viability and the performance against previous Plans vary between the different constituent businesses. Our conclusions on the constituent businesses may be summarised as follows:

Austin Rover Group Holdings

5.2 The Plan for ARGH is broadly unchanged from last year. Achievement of the Plan is crucially dependent on the launch of the LM10 and LM11 within the next 18 months, and on the further development of collaborative links with Honda. Nonetheless, it is clear from the Plan that on current projections ARGH on its own will not become commercially viable within the Plan period, although the prospects for some sort of joint venture with Honda may be better. There must be considerable doubt about whether ARGH, in isolation from the rest of BL, could generate or borrow on its own surety sufficient funds to finance the model replacement programme which will become necessary in the late 1980s, and which will involve heavy capital expenditure just beyond the Plan period. This problem has been recognised for some years, but it is brought out more starkly in this year's Plan than previously because of the separate identification of forecasts for Jaguar, which had previously tended to obscure the position of ARGH within the Cars Group.

5.3 The poor results projected for ARGH suggest strongly that further action needs to be taken to resolve the issue. BL propose in the Plan a number of options for such action, and it is clearly important that these options are further developed as a matter of urgency. We know that Mr Ray Horrocks has in mind a wide-ranging review of the ARGH business next year some months earlier than would be necessary for the 1984 Plan, and this review will of necessity involve closer examination of the options which BL have identified. Given this review, and that the measures of privatisation (of Jaguar and Unipart) which would trigger the problem are unlikely to occur before 1984, and that the model replacement programme which is at the root of the problem will not take place until the late 1980s, we conclude that a detailed evaluation of these options can as BL propose await the 1984 Corporate Plan. It will however be important to ensure that any agreement about future collaboration reached in the meanwhile between ARGH and Honda does not prejudice any of the options.

Jaguar Group

5.4 The dramatic turn-round of the company has continued, and the company is well on course to commercial viability. If anything, we believe that the Plan slightly understates the prospects for Jaguar.

Unipart Group

5.5 The prospects for SU Butec, the Group's manufacturing operation, appear reasonable and are based on prudent assumptions. Achievement of the Plan for Unipart Division, the replacement parts marketing operation, depends crucially on achieving a substantial growth in sales in a more or less static "all makes" market. This will not be an easy task, and there must be a risk that the targets in the Plan will not be met. Nonetheless, we conclude that the Plan presents reasonable prospects of commercial viability for the Unipart Group as a whole.

Land Rover Group

5.6 The environment in which LR operate has not improved since last year, and may well have deteriorated. Economic difficulties abound in LR's traditional markets, and competition is intense. There are clearly risks to the achievement of the Plan. We are not convinced that sufficient management attention has in the past been paid to addressing these risks, but there are now signs - for instance, the attention which is now being paid to the company's product strategy - of the increased effort in this area which we believe to be necessary if the Plan is to be achieved. This increased management effort, together with the launch next year of the Stage 2 Land Rover, gives reasonable grounds for expecting that the company will be able to build on its well-established reputation and its good products and remain one of the more profitable parts of BL.

Leyland Group

5.7 The 1982 Plan for Leyland Group was admitted to be subject to substantial risks. Most of these risks related to Leyland Trucks, whose projections in several important areas, notably profitability, market share and productivity, have been missed. Although all European truck manufacturers have been experiencing a difficult year, there is clearly a major task ahead for Leyland Trucks, including making up the ground that has been lost against Plan this year. Experience so far does not suggest that the risks are any less than they were last year although they cannot be said to be any greater. Some economic indicators, notably the exchange rate, have moved in Leyland's favour although the intense competition from other manufacturers shows no sign of abating. The prospect of viability remains more or less the same as it was last year. Leyland Trucks' recovery is crucially dependent on how the market receives its new model ranges, the MT207 (the launch of which started this Autumn) and the MT211 (due to be launched in 1984). We shall need to continue to monitor performance very closely and the "benchmark" system will help us to pick up any adverse developments at an early stage. Meanwhile, the performance of the Group as a whole has been affected by problems in its overseas subsidiaries, although these problems do not appear to call for action as drastic as was needed for Leyland Trucks.

Privatisation

5.8 The privatisation strategy included in the Plan, although its detailed implementation has not yet been worked out, presents reasonable prospects for visible progress towards privatisation in the next two years. The firmest candidates are Jaguar and Unipart. A strategy has been produced for privatising Land Rover and Leyland Groups together by 1985, but we have reservations about whether this is the best strategy available. We therefore believe that BL should be required not to take any steps which would make the privatisation of Land Rover on its own more difficult to achieve. The prospects for privatising ARGH are poor, but BL are undertaking a review of the available options for ARGH and it should be possible to take a firmer view at the time of the 1984 Corporate Plan. The privatisation strategy which BL have prepared for the 1983 Plan is not a detailed timetable for privatisation, but in the light of all the commercial uncertainties we believe that it goes as far as possible towards demonstrating how privatisation is likely to proceed. We provisionally conclude, therefore, that the strategy fulfils the commitment given in Sir Michael Edwardes's letter of 4 August 1982, although progress towards its implementation will need to be closely monitored by the Department of Industry.

Funding

5.9 The 1981 and 1982 Corporate Plans envisaged the provision by the Government in 1983-84 of £150m equity in addition to the £990m which the Government agreed to provide in 1981-83. Of this £990m, £780m has already been drawn down, and it is probable that another £60m or so will be drawn down by the end of the financial year, leaving £150m to be rolled over to next year. However, in this Plan BL are seeking a further equity injection of £100m, not £150m as previously envisaged, making a total of £250m likely to be paid in 1983-4. This £50m reduction in BL's equity requirement is in anticipation of the proceeds of privatisation, although these proceeds will not be available during 1983-84 and BL will need to resort to extra borrowing as an interim measure.

5.10 The 1981 Plan projected a cash outflow over the period 1981-5 of £1526m, of which it envisaged that £1140m, or approximately 75%, would be covered by Government equity. The cash outflow for the same period projected in the 1983 Plan is somewhat lower, at £1445, but the proportion of this which it is proposed should be covered by Government equity remains at about 75% as a result of the reduction in BL's request for equity.

5.11 A series of statements on the Government's attitude to BL's obligations (the Varley-Marshall-Joseph statements) have made it clear that in the event of BL's being unable to meet its obligations they would be assumed by the Government. This undertaking creates a contingent liability on the Government in respect of BL's borrowing and creditors. BL's total borrowings at present amount to a little over £900m, and creditors to a little over £700m, and these totals are projected in the Plan to rise by 1987 to over £1000m and nearly £1150m respectively. The Government's contingent liability might therefore increase by as much as £550 over the Plan period, although this may be offset by any increase in the value of BL's assets. However, as privatisation proceeds those companies which are privatised will subsequently trade and borrow as commercial companies on their own surety, and this will tend to reduce the Government's maximum exposure.

?

Recommendation

5.12 The performance of and prospects for the component companies of BL are extremely variable. Some companies (eg Jaguar) are well on course to earning a commercial return in the next few years, and there are good chances of early privatisation. For others (eg Leyland Group) the prospect of a recovery is less certain. ARGH is unlikely to achieve commercial viability within the next decade as a wholly independent company, although the prospects for some sort of joint venture may be better. Nevertheless, in all parts of the company the investment of the last few years is starting to bear fruit as new model ranges come on stream. For the first time in many years, BL are not expecting any further Government equity beyond that they are requesting for the year ahead. BL have always argued that there would be a need in 1983-4 for a final injection of Government equity in order to enable the company to complete this recovery programme. We accordingly recommend that BL's request that £100m of equity should be made available in 1983-4, over and above the £150m or so of the £990m previously agreed which is likely to be rolled over to that year, should be approved. (Because of the uncertainties of cash forecasting, we cannot preclude the possibility that some part of this equity might fall to be paid in 1984-5). The provision of equity would of course be subject to performance and demonstration of need. Any substantial failure to meet the major financial targets of the 1983 Plan is covered by Sir Michael Edwardes's letter of 26 January 1981, a copy of which is attached at Annex 3.

ANNEX I

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BL PERFORMANCE IN 1982

I INTRODUCTION

1 This comparison of performance in 1982 with that projected in the 1982 Plan takes as its starting point the forecasts for 1982 continued in the 1983 Plan. These were made on the basis of the year to August (the "8 + 4" forecasts); more recent forecasts (the "10 + 2" forecasts) are now available, and are referred to where appropriate; significant differences arise in the case of cashflow and capital expenditure, and these are explained below. This Annex continues with the classification of the Groups employed in the 1982 Plan: the 1983 Plan and latest forecasts are on the basis of the Groups as now reconstituted. Cars Operations consists of Austin Rover Group Holdings and Jaguar (the old Cars Group, but with BL Technology added to ARGH) and Unipart. Land Rover-Leyland consists of the two Groups unchanged, and both separate and combined financial tables are given in the 1983 Plan.

II ECONOMIC BACKGROUND TO 1982 PERFORMANCE

2 The Inter-Departmental Group paper on the 1982 BL Corporate Plan considered that on the general level of activity BL were "relatively pessimistic" but that, overall, the economic assumptions

forecast seemed "reasonably central". In the event, by contrast with 1981, BL's view of the world was fairly well borne out. UK competitiveness benefited from lower than expected inflation. On the other hand, until recently the pound remained strong against European currencies; and a faster than expected reduction in UK-European price differentials kept up pressure in a domestic car market already characterised by intense competition.

3 The state of the UK and world cars and commercial vehicle markets are considered below. BL's own projection of these, and the latest forecast outturn, are as follows:-

UK markets: Total industry volumes (TIVs)

(000s)	10 + 2 forecast	Plan	Memo: 1981
Cars	1549	1455	1485
Car derived vans	62	55	59
Light Commercial (PV2 Sector)	57	56	53
Trucks	45	40	45

III PROFITS, REVENUE AND COSTS

4 PBIT in 1982 is expected to be better than Plan for BL. This is entirely due to the performance of Cars Group, with the other Groups performing rather below Plan. However, in all cases, revenue is below budget - as a result of lower volumes or margins or both - so that even Cars Group owes its PBIT performance to reduced costs.

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		Cars	Unipart	Leyland	Land Rover	BL*
Revenue:	(£m)	1740	335	797	438	2978
Better/(worse) than Plan		(62)	(64)	(122)+	(38)	(302)
PBIT:	(£m)	(105)	11	(29)	8	(134)
Better/(worse) than Plan		17	(2)	(38)+	(4)	11
Retained Earnings	(£m)	(181)	4	(41)	(10)	(301)
Better/(worse) than Plan		43	(2)	(24)	(5)	19
Economic profit/ revenue	(%)	29	28	21	30	30
Better/(worse) than Plan		3	3	(2)	1	2
Fixed costs less dep'n/ revenue	(%)	30	24	22	24	30
Better/(worse) than Plan		(2)	(2)	(4)	(1)	(2)
Sales volumes	(000)	423	NA	49	66	517
Better/(worse) than Plan		(26)		(3)	(3)	(32)
Market share UK	(%)	18	NA	14	NA	NA
Better/(worse) than Plan		(2)		(2)		

*Total BL figures include other companies, Leyland Group contingency provision and central consolidation, not shown separately.

+The effects of these shortfalls on the total BL figures were mitigated by the inclusion in the Plan of central contingency provisions against such shortfalls, of £52m revenue, £40m PBIT.

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5 The following table summarises BL's explanations of PBIT variance from Plan in 1982, based on the 1983 Plan forecast for 1982. The table shows that PBIT in 1982 will be better than Plan for BL as whole, entirely due to better than Plan performance from ARGH and Jaguar, partly offset by varying shortfalls in other parts of BL. Although a better than Plan performance is indicated for Leyland Group, this result only appears after using up a £40m PBIT central contingency and, moreover, does not reflect the latest forecast which suggests a somewhat worse performance.

Analysis of 1982 PBIT variance from Plan (£m)

Explanation	BL	ARGH	Jaguar	Unipart	Land Rover	Leyland	Other
UK Demand	(22)	-	-	(16)	-		-
Pricing	)	-	-	-)	)	)	-
	) (7)			)	(6)	) (6)	-
Exchange	)	(3)	8	-)	)	)	-
Cost performance/ market share	45	13	(1)	14	8	13	(2)
Export volume	(5)		-	-	(6)	1	-
TOTAL	11	10	7	(2)	(4)	2	(2)

IV CASHFLOW AND ASSETS

6 The cashflow and asset position is summarised in the following table:-

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		Cars	Unipart	Leyland	Land Rover	BL*
Cashflow in/(out)(£m)		(320)	(10)	(130)	(46)	(524)
Better/(worse) than Plan		14	(12)	(33)*	(6)	33
Capital expenditure	(£m)	(142)	(11)	(58)	(40)	(267)
Lower/(higher) than Plan		21	(2)	(1)	8	49
End-year working capital	(£m)	209	122	189	99	622
Lower/(higher) than Plan		28	23	(5)	10	62
End-year total assets	(£m)	710	159	432	267	1620
Lower/(higher) than Plan		79	20	22	15	135
Manpower	(000)	48	5	31	14	103
Lower/(higher) than Plan		4	1	-	2	9

*A provision of £55m was made centrally against such worse than Plan Leyland Group Cashflow.

7 This table is based on the "8 + 4" forecasts, those contained in the Plan. However, following a detailed review of expenditure to date, BL estimate that capital expenditure in 1982 will probably now total no more than £235m, compared with £267m shown in the 1983 Plan and £316m forecast in the 1982 Plan. The 1982 budget contained an aditional £54m capital expenditure deferred from 1981. Altogether BL estimate that about £95m unspent in the 1981 and 1982 capital programmes will be re-phased into later periods. The company have stressed that no major capital programmes have been delayed, and believe that these programmes will, over time, incur the same total expenditure as envisaged in the 1982 Corporate Plan.

8 Working capital ended 1981 at a level below that assumed in the 1982 Corporate Plan, largely owing to lower Cars Group inventory as a result of the strike. Whilst this Cars Group shortfall had to be made up to some extent over the year, the whole company is still expected to finish 1982 with a lower than Plan working capital level. Although the latest (10 + 2) forecast is for a £50m lower end-1982 working capital than is assumed in the 1983 Plan, at £572m, there is an element of risk to the achievement of the Leyland Group forecast, which depends on certain export shipments getting clearance before the end of the year.

9 This cashflow is being funded by a combination of equity and medium-term loans, with short term borrowings being run down. At the end of 1981, BL negotiated £277m of new medium term loans, £202m of which has now been drawn down. To some extent, these were to replace short-term borrowing which had for some time been providing, in effect, medium-term finance. £260m of equity finance was provided during the year, £180m in October and £80m in December.

IV CARS GROUP

10 Until hire purchase controls were abolished in July, the UK market for cars was running 2% below the already depressed 1981 level. Since then the added stimulus of falling interest rates has given the market a much-needed boost which is likely to carry over into 1983. But markets elsewhere in Europe have been depressed all year, with competition correspondingly intense and sales offering a low return. The relative strength of sterling compared with other European currencies has made Britain an attractive place in which

to sell cars. Foreign producers, with their lower production costs have been able to hold down prices to maintain or even improve market share while still getting a better return than in Continental Europe. UK manufacturers have been obliged to join in the price-cutting war though less well-placed to do so because of their higher production costs. Despite having to spend money on discounts to dealers and marketing campaigns, Cars Group have managed to keep total costs within Plan levels. As a result, they have shown a slightly better than Plan PBIT, coming from slightly lower than Plan revenue. Because the growth in the UK market has been most marked in the upper medium sector, where BL's product range is weakest, they have not fully benefited from the larger market and their share has been less than Plan. Metro, which held on to its share of the small market sector, also had a lower then Plan share of the total market.

11 Jaguar has benefited from the strong dollar and from great improvements in perceived quality. Following the reorganisation of BL in October, seperate figures have become available for Austin Rover Group Holdings (ARGH) and Jaguar. The 10 + 2 forecasts are thus not directly comparable with figures for the old Cars Group, because of inter-company trading (which does not of course show up when the transactions take place within a single Group) and the addition of BL Technology to ARGH, but they illustrate the variation in Jaguar and ARGH performance.

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Jaguar

	F'cast	b/(w) than budget	
PBIT £m	12.5	8.8	(F'cast = 338% of budget)
Revenue £m	312.9	46.7	(F'cast = 118% of budget)
Export revenue £m	167.0	34.1	(F'cast = 126% of budget)
PBIT/revenue %	4.0	2.6	
PBIT/assets %	12.3	8.8	
Unit wholesales 000	21.5	2.0	(F'cast = 110% of budget)
Cashflow £m	(26.5)	16.6	
Capital expenditure £m	39.1	(9.1)	
EP/sales %	28.7	0.9	
FC/sales %	22.4	(0.4)	

Austin Rover

PBIT £m	(115.0)	23.1	
Revenue £m	1512.0	(88.6)	(F'cast = 94% of budget)
Export revenue £m	209.0	(58.5)	(F'cast = 78% of budget)
Unit wholesales 000	398.7	(34.1)	(F'cast = 92% budget)
Cashflow £m	(225.8)	183.5	
Capital Expenditure £m	101.2	(66.2)	
EP/sales %	29.3	3.8	
FC/sales %	31.5	(3.5)	
Market share	17.3	(2.2)	

VII UNIPART

12 The profit shortfall appears to have arisen in the parts business, with the component manufacturing business (SU Butec) performing satisfactorily. Both export and domestic sales have been affected: exports by economic difficulties in major Middle Eastern and African markets, domestic sales by the loss of distributors, and destocking, as a result of the economic climate and lower car sales in the past which have hit current demand for parts. An attempt to break into the market served by independent "factors" (who hold stocks of parts for supply to small garages) through the "Express Factors" scheme has met with some initial success, but has not yet gained widespread participation.

VIII LEYLAND GROUP

13 In 1981, sales of commercial vehicles were depressed worldwide, but were particularly so in the UK where they slumped 20% below the already depressed 1980 level. The limited recovery in 1982 has been concentrated primarily in the van sector, sales of trucks remaining severely depressed. Competition for sales has been understandably intense, with importers better able to hold or reduce prices as a result of their lower production costs and the relative strength until recently of the pound.

14 The following table gives latest forecast performance for Leyland Group broken down into its principal UK operations, Leyland Vehicles Limited (LVL), and the major overseas subsidiaries, in India and South Africa. The Leyland Truck division of LVL is also identified separately.

	Leyland Truck	LVL*	Ashok (India)	South Africa	Other	Leyland Group
PBIT £m	(70.0)	(53.5)	13.7	7.3	(4.7)	(37.2)
B(w) than budget	(15.1)	(25.2)	(7.4)	(7.0)	(6.5)	(46.1)+
Revenue £m	289.7	410.8	163.9	85.8	5.1	665.6
B(w) than budget	(77.1)	(92.7)	(75.2)	(71.5)	(14.2)	(253.6)+
Sales volumes 000	15.5	Not available				41.3
B(w) than budget	(2.2)					(11.1)
Cashflow £m	(80.4)	(81.9)	(30.6)	(8.4)	(14.6)	(121.5)
B(w) than budget	(10.2)	(25.4)	(6.2)	(2.5)	(12.7)	(46.8)+
Capital expenditure £m	Not available					46.4
More (less) than budget						(37.8)
Market share %	13.3		NA			NA
B(w) than budget	(2.5)					

*Includes Truck, Parts, Bus and consolidations.

+Contingencies were held centrally, to offset performance shortfall, of £40m PBIT, £52m revenue and £55m cashflow.

15 It is apparent from this that LVL, where the performance shortfalls were expected to occur (against which central contingencies were provided in the 1982 Plan), is only responsible for just over half the expected PBIT shortfall, and two thirds of that on cashflow. The bulk of the residual shortfalls occur in the two major overseas operations. These, although consolidated into Leyland Group, do not rely on the centre for funding.

16 LVL's financial results were affected by, among other things, the four-and-a-half-week strike in January and February at Leyland Vehicles plants, over restructuring plans. This ended with the acceptance by the workforce of these plans and their associated redundancies in full, since when the workforce has cooperated fully in the implementation of the measures. This is not to say further problems may not arise as restructuring continues; but the real risk of a total breakdown in workforce co-operation (seen in the 1982 Plan) seems to have receded. A number of other factors have combined, however, to prevent Plan targets being achieved for the remainder of the year. With the UK Truck market now expected to be, at 45,000, no higher than in 1981 (albeit better than BL's Plan assumption), pressure on prices has been intense, and is particularly acute in the case of the older models on which LVL has had to rely heavily for its sales. This lack of a complete modern product range is gradually being rectified, with the replacement for the Boxer light medium truck launched in October; the replacement for the Terrier light truck, in a sector of the market taking a third of UK

sales, will be launched in 1984. Both market share and profitability have therefore to be seen in the context of the lack of a full, competitive, product range. Export sales have also suffered from the economic difficulties of major African markets, for example Nigeria which is now expected to take only 1,800 of a predicted 3,300 sales in the year. The necessary restructuring of truck production - involving the concentration of production onto three sites - and in particular the expansion of assembly at Leyland, has caused some temporary dislocation, resulting in failure to meet supply targets. Where there are already established new models - in the medium and heavy range - however, demand has been good. Despite the intense competition, profitability targets are now beginning to be met, owing, to a large extent, to successful control of material costs.

IX LAND ROVER

17 The PBIT shortfall is due to a change in the pattern of Land Rover Ltd's sales in 1982: although total sales are only expected to fall off slightly, the mix has changed in favour of European markets where margins are lower than in the Third World. African and Middle Eastern sales were affected by the economic and political problems of certain oil-producing countries, such as Nigeria and Iran, both major markets. These factors mean that the current forecast profits must be placed in doubt, despite the prospect of overall sales at or near Plan levels.

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18 Freight Rover sales have been satisfactory, following the launch in June of the remodelled Sherpa van, and the recovery of the van market. Freight Rover have been making trading losses within budget and are expected to be trading at breakeven by the year end.

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ANNEX 2

REGIONAL IMPLICATIONS

The regional implications of the Corporate Plan arise both out of BL's own closure plans and out of the effect on component suppliers of any resourcing by BL.

BL Closures

2 Closures or partial closures are planned for plants which fall within the Birmingham and Bathgate Travel-to-Work Areas (TTWAs). In addition the future of plants within the Coventry and Bristol TIWAs are to be subject to review. Table A illustrates the sort of impact that these closures will have on the unemployment rates. Closures in Birmingham, Coventry and Bristol will not, on their own, lead to a marked deterioration in the unemployment rate or undue pressure for Assisted Area status (all these areas are currently non-Assisted).

3 The closure at Bathgate in late 1984 would have the most serious regional implications. Unemployment in the TTWA - already high at 22.5% (October) - would rise by nearly 2%. The current average for all Special Development Areas (SDA) is 19.1%. Part of the TTWA - Livingston New Town - is already an SDA; the remainder is a Development Area. There would undoubtedly be further pressure for uniform SDA status. The Government have however given a

public commitment not to make further changes in the Assisted Area map during the rest of this Parliament other than in the most exceptional circumstances.

Component sourcing

5 Any significant switch by BL to overseas sourcing for their components would undoubtedly affect the West Midlands. It is impossible to estimate the likely effect on such places as Oakengates (current unemployment rate 20.5%), Walsall (18.9%), Coventry (17.6%) and Birmingham (18.0%) without precise knowledge of the suppliers which are most at risk and their location. If a change in BL's component sourcing policy led to any significant increase in unemployment in the area, there could be further political pressures to grant Assisted Area status to parts of the region.

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TABLE A

ESTIMATED EFFECT OF BL CLOSURES ON UNEMPLOYMENT RATES

TTWA	Unemployment October 1982 Nos	%	No of Redundancies	Post closure unemployment (based on October '82 figures) Nos*	%*
Birmingham	125,788	18.0	minimal	Not known	18.0
Coventry	42,642	17.6	270	42,858	17.7
Bristol	36,628	11.2	633	37,134	11.4
Bathgate	11,175	22.5	1,000	11,975	24.1
all SDAs	-	19.1	-	-	-
all DAs	-	16.6	-	-	-
all IAs	-	15.8	-	-	-
GB	-	13.6	-	-	-

* - assuming that all the redundancies had already taken place, and that only 80% of those made redundant had claimed unemployment benefit.

ANNEX III

RECEIVED IN
26 [illegible]
SECRETARY OF STATE
FOR INDUSTRY'S OFFICE

TELEPHONE 01-486 6000

35-38 PORTMAN SQUARE
LONDON W1H 0BN

FROM SIR MICHAEL EDWARDES

26th January 1981

TO Mr Bender
PLEASE BY:
Noon
2/2/81.

COPIES TO
PS/MT
PS/MM
PS/PS
Mr Steele
Mr Mountfield

The Rt.Hon. Sir Keith Joseph, Bt,MP,
Secretary of State for Industry,
Ashdown House,
123 Victoria Street,
London SW1.

Dear Secretary of State,

The Board believes that BL's 1981 Corporate Plan offers - subject to the risks and qualifications which are made clear in the Plan - the best feasible prospect of bringing about the recovery of the business.

As you know, recovery will take time, and during this period the risks to the survival of whole sections of the business will remain considerable. While it should be possible for the business to accommodate the normal trading fluctuations within the framework of the Plan, the achievement of competitive cost levels is essential to ensure our survival. As we have made clear in recent weeks, even the success of a particular new model such as Metro cannot allow us to relax the strict discipline which has to be exercised on all aspects of our cost structure.

Government approval of our Plan and funding request would not change this situation, because it is our own performance in the external competitive environment which fundamentally determines whether or not the business can survive. Dealers and customers would simply walk away from the company if there were a major strike. Moreover, they would desert us more gradually, but no less surely, if we allowed our costs to rise to uncompetitive levels - or indeed if it seemed to them that the necessary funds would not be sought from Government.

Continued

Circumstances may arise in which, through a substantial deviation in performance or an appreciable departure from the assumptions underlying it, the Corporate Plan is clearly not being achieved and it appears impossible to bring about recovery within the timescale envisaged. This could arise for external or internal reasons; an example would be a major strike which damaged or appeared certain to damage any substantial sector of the business. In such circumstances the Board would, in accordance with section 1 of the Plan, very quickly initiate a review (in consultation with the Government) of the Plan of the relevant business group, with consequent implications for continued Government funding.

The Board will, of course, be monitoring progress under the Plan regularly in the normal course of its business and in the context of the annual updating of the Plan towards the end of 1981.

In our recent discussions on the Corporate Plan, you also asked me to confirm to you the views of the BL Board on the importance of collaboration in our recovery strategy for each of our main business groups.

The Board sees collaboration with other manufacturers as an important part of its strategy for recovery and for reducing and eventually removing dependence on Government support. This might take the form of collaborations on major components or on particular parts of the business; but the Board would also welcome, and actively seeks, a relationship of a more comprehensive kind which might well grow out of such collaboration.

Yours sincerely
Michael Edwardes.

ANNEX 8

35-38 PORTMAN SQUARE

LONDON W1H 0HQ

FROM SIR MICHAEL EDWARDES

4th August 1982

The Rt.Hon. Patrick Jenkin, MP,
Secretary of State for Industry,
Ashdown House,
123 Victoria Street,
London SW1.

CONFIDENTIAL

Dear Secretary of State,

Further to the very constructive meeting which you had with the BL Board on 6th July, it may be helpful if I confirm the Board's position on the matters we discussed.

With regard to privatisation, I confirm that it is the Board's objective to return BL in whole, and probably by instalments, to the private sector as soon as practicable. We acknowledge the wish of Government to show early and visible progress to this end, consistent with maintaining the recovery strategy in the Corporate Plan.

Prior to the meeting, we had tabled for illustrative purposes a profile indicating one of the possible routes to full privatisation which will be examined in the privatisation strategy which is being developed for the 1983 Corporate Plan. Until the necessary studies for the 1983 Plan have been completed, it would be unproductive to try to set out the other available options for achieving a return to the private sector or to be more specific about the individual actions which will comprise each option. However, the Board believes

Continued.. ..

the Board believes/

that it can offer a broad commitment to the Government on certain issues, based on the following assumptions:-

1. that the Board will be able to appoint one of the present non-executive Directors as Chairman * (I am now putting to the Board the formal proposal that Sir Austin Bide and Sir Robert Hunt should be appointed non-executive Chairman and Deputy Chairman respectively);

2. that the Government consequently approves the Board's proposals for succession which provide for the maximum continuity at Board and top management levels;

3. that an objective on the lines set out in my second paragraph above will be agreed between the Board, the new Chairman and the Government;

4. that the Government does not proceed with its proposal for the total disposal of Land Rover, while satisfactory progress is being made towards the achievement of (a) and (b) below;

5. that, subject to approval of the 1983 Corporate Plan, the Government agrees to provide, in addition to the £990m already committed, such part of the £150m equity funding envisaged in previous Plans for the period after March 1983 as is not offset by estimated proceeds from the sale of minority interests (see (a) and (b) below) and which can be demonstrated to be needed to fulfil the Plan; and

6. that the major financial targets in the current Corporate Plan are broadly achieved each year, as is expected to be the case for 1982 - non-achievement is of course covered by my letter of 26th January 1981 to your predecessor.

Continued..

* All the directors support it in fact. M.

On these assumptions, the Board commits itself firmly to the following specific objectives within the overall objective enunciated above:-

(a) To limit BL's requirement for Government funding to the amounts referred to in 5 above. This will mean that the final £150m funding requirement envisaged in previous Plans should be significantly reduced and that, subject to receipt of the balance of the funds already approved by the Government, there will be no further Government funding requirement for maintenance of the business after the financial year beginning in April 1983. The only circumstances in which Governmer funds might be needed thereafter would be:-

i. In the event of a total or partial collapse of the business, the Varley/Marshall/Joseph assurances that the Government will meet BL's obligations would be triggered; the Board sees no possibility of the Government being relieved of these assurances until full privatisation is complete, but the Board will explore the practicality of reducing the scope of the assurances, e.g. the possibility that in conjunction with the sale of minority equity stakes certain subsidiaries might be able to borrow externally on their own account without the comfort of the assurances.

ii. We have an unacceptable balance sheet for private sector purposes, and as we privatise we will need to remedy the position for those companies taking on outside shareholders or joining the private sector. There might be a need for Government finance immediately prior to privatisation, but the aim would be at least to recover any outlay by the proceeds of dispos als

Continued.. ..

(b) To devise a strategy for full privatisation in the 1983 Corporate Plan which offers visible progress within the next two years towards privatisation by such means as the sale of minority equity stakes in BL's more profitable businesses; which builds on existing collaborative arrangements (such as Austin Rover/Honda)) and seeks new opportunities for collaboration (such as the informal approaches we have made to International Harvester, DAF and more recently Volvo about links with our commercial vehicles business) in order to make BL's constituent businesses more attractive for ultimate privatisation; and which maps out possible routes for the full return of all parts of BL to private ownership by the late 1980's, setting target dates wherever possible.

(c) To make a public statement this autumn (if possible at the press conference for BL's half-year results on 15th September) underlining the Board's commitment to privatisation. A draft of such a statement is attached.

Yours sincerely
Michael Edwardes

Enc:

FOR HALF YEAR STATEMENT

PRIVATISATION

As I said in my report to shareholders in March of this year, the division of BL into separate operating units increases operating efficiency and also makes it easier to inject private sector funds into some or all of these businesses when they reach a commercially attractive stage. The Board now feels that with the continuing progress being made towards profitability, it is realistic to seek private sector funds over the next two years for BL's mainstream businesses. The Board sees these developments as the first step towards an eventual return of BL to private ownership.

Private sector funds, coupled with the continuing progress of the businesses, would, the Board believes, enable it to bring forward the time when the Company can sustain itself without Government funding. The 1983 Corporate Plan will be submitted on this basis. The Board envisages that the final £150m of Government funding required in the 1982 Plan will be significantly reduced, thus bringing this funding to an end earlier than expected in previous Corporate Plans.

30.7.82

ANNEX C

679.1

In the case of the Austin Rover Group Plan, the Government's approval has been given on the understanding that Ray Horrocks has in mind a wide-ranging review of the Austin Rover business next year some months earlier than would otherwise be necessary for the 1984 Plan, and that this review will involve close examination of the options for this business which the BL Board have identified in the Foreword to the 1983 Plan.

In the case of the Leyland Group Plan, the Government's approval has been given on the basis that BL have in mind that the progress of Leyland Trucks in 1983 will continue to be measured against certain "benchmarks", and that progress against these benchmarks will continue to be monitored by my Department as part of the monthly monitoring arrangements for BL as a whole.

In the case of Austin Rover, of course, the Corporate Plan's proposals for privatisation are inevitably somewhat limited. No doubt the complete privatisation of Austin Rover will take longer than the other parts of the business, but it is important that we turn our attention now to a strategy for privatisation including first the reduction and then the ending of Government support via the Varley/Marshall assurances on borrowing. I would hope that Ray Horrocks' review could incorporate consideration of these points. In particular, it would be useful if BL could study possible alternatives to the Government assurances, including possible changes which might over time reduce the Government's exposure under these assurances even before privatisation. A progressive collaboration with Honda would appear to us to be the most likely way of ending Austin Rover's dependence on the Government, and I should be grateful if everything possible could be done to enhance the prospects of this.

I have noted the BL Board's preference for privatising the Land Rover and Leyland Groups together by 1985. While not prejudging the issue in any way, but given the uncertainty of the prospects for the Leyland Group, I should be grateful if the Board would not proceed now with any measure which would make privatisation of Land Rover on its own in 1984 or 1985 more difficult to achieve. In addition, I should be grateful if you and your staff could continue to keep my Department closely informed about progress towards implementation of the privatisation strategy for BL's various businesses.

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