



10 DOWNING STREET

3 April 1985

From the Principal Private Secretary

Dear Calum,

BRITISH LEYLAND

Your Secretary of State came for a further discussion with the Prime Minister this afternoon. The Financial Secretary to the Treasury was present as were Mr Gregson (Cabinet Office), and Mr Warry (No 10 Policy Unit).

Your Secretary of State said that there had been some further developments since the discussion which he had had with the Prime Minister earlier in the week. Firstly, it had to be remembered that, whether or not the negotiations with GM for the sale of Land Rover Leyland went ahead, it was likely that at least Land Rover/Range Rover could be sold and this would reduce the Group's capital expenditure by £196 million by 1989, as well as bringing in the proceeds of the sale. Second, he had spoken to Sir Austin Bide and Ray Horrocks, and the latter had agreed to see how near he could get to cutting £250 million off the capital expenditure of Austin Rover. But, since the Corporate Plan had been prepared, the emissions directive had been agreed and this was expected to have an adverse effect on their cash flow of £200-250 million over the period, which was roughly evenly divided between the cost of adapting vehicles and the effect on product development and sales. Third, rumours of the Honda deal were breaking in Japan and the Chairman of Honda would be coming over in the following week. The proposals covered joint model development, a unit at Swindon at which Honda would manufacture the 1.3 engine and Honda's use of facilities at Longbridge for production and assembly. Bringing the facilities into use by Honda at Longbridge would require additional capital investment estimated at £22 million in 1986, £71 million in 1987, £73 million in 1988 and £17 million in 1989 before the effect on British Leyland became positive. British Leyland would have to make some response to the approach by Honda and the tone of this response would be crucial: the Government had therefore to decide whether in principle it wished to encourage the proposed deal between British Leyland and Honda or not.

In discussion, it was pointed out that no precise details of the proposed agreement between BL and Honda were available and the financial effects on BL's Corporate Plan would have to be very carefully considered before the Government could take a view about the merits of the

proposals. It was not clear why BL rather than Honda needed to incur the investment to bring the production facilities at Longbridge into use. Nor was it clear how much Honda were directly investing overall. There were dangers that they were getting a further foothold in the British motor market at minimum cost to themselves. On vehicle emissions, the company's claim that compliance with the directive would cost them substantial sums also needed close examination: if they were to adopt established Honda engines instead of developing the new engine which they envisaged, the cost could be much reduced. The effect of all these developments on the Corporate Plan needed to be carefully considered, together with the treatment of the proceeds of the sale of Land Rover/Range Rover. On the other hand, it was pointed out that the Government had encouraged BL to seek collaborative ventures on new models and Honda's proposal to manufacture their 1.3 engine at Swindon was attractive. All that was necessary at this stage was to determine the tone which BL used in responding to Honda's approach.

Summing up the discussion, the Prime Minister said that the Government did not have sufficient details, and particularly financial details, to form a view on the merits of the Honda approach. She was not prepared to authorise any commitment to Honda's proposals at this stage: personally she was very sceptical about them. All that could be said was that the Government would consider any specific proposition, provided that the effects of the various developments which were under discussion on the BL Corporate Plan were clearly set out. The Government might well require an examination of these by independent experts. She would be prepared to meet the Chairman of Honda at some stage, but at present the proposals were so unprecise that it did not look likely that there would be a sufficient basis for such a meeting on his forthcoming visit.

I am copying this letter to Rachel Lomax (H M Treasury) and Richard Hatfield (Cabinet Office).

Your ever,

Robin Butler

Callum McCarthy Esq  
Department of Trade and Industry