

File



10 DOWNING STREET

From the Private Secretary

24 May 1985

BRITISH LEYLAND

There are one or two points which emerged from yesterday's meeting which I have not included in the record which has been sent to all members of E(A). Your Secretary of State said he expected to hear before the end of next month on the outcome of negotiations with GM. Although there were other potential buyers for parts of Land Rover-Leyland, he did not think it right to enter into negotiations with them until talks with GM were either completed or had broken down. This was not challenged at the meeting, though I do not think this necessarily implies that the Prime Minister has abandoned the view expressed in my letter of 11 March that other buyers should be sounded out against the contingency that GM do not acquire LR-L or wish to acquire only parts of it.

Your Secretary of State said that by the end of the year he hoped that Unipart and much of LR-L would have been disposed of. This would make it unnecessary to divide BL into two separate entities. At this point he proposed to bring about major changes in the composition of the BL Board. It was noted that while the disposal of Unipart would not trigger renegotiation of BL's loan stock, disposal of LR-L probably would.

Andrew Turnbull

CST

John Mogg, Esq.,
Department of Trade and Industry.

cc Master Set

SECRET

FILE

2.

JCAAPM



cc PGO D/M SO
 CO CAL D/N
 DOT WPSO NIO
 CST DOE HMT
 MAFF WO MWP
 ce fw.

10 DOWNING STREET

From the Private Secretary

24 May 1985

Dear John,

BL CORPORATE PLAN

The Prime Minister held a meeting yesterday to discuss the BL Corporate Plan. Present were the Secretary of State for Trade and Industry, Chancellor of the Exchequer, Minister Without Portfolio, and Minister of State for Industry. Mr. Wiggins (Cabinet Office) was also present.

The Prime Minister said that although BL's Corporate Plan did not imply any further injection of cash from the Government, she was very concerned, particularly given under performance of previous plans, at the growth of the company's borrowings and at the growth of total liabilities subject to the Varley-Marshall assurances. Borrowings were expected to rise by £220 million in the course of 1985 and over the next five years total liabilities were projected to rise by over £500 million to around £2 billion. Every effort should be made to reduce these totals and, where possible, limits should be set on them.

In particular BL's plan to develop a new small engine itself - the K series - should be seriously questioned. She doubted whether it made sense for ARG, as a volume producer, to make its own engines. Before agreeing to the Corporate Plan she wanted to be satisfied that a suitable small engine could not be acquired from Honda. She believed Honda would be able to supply an engine for the Metro replacement which would meet European emission standards at an acceptable level of performance. The meeting on the Memorandum of Understanding implied that it was reluctance on the part of ARG rather than willingness of Honda to supply that was the obstacle to this course. The Prime Minister did not believe that any weight could be put on the Barings Report. At numerous points in the report caveats had been made that the

SECRET

authors had not been able to analyse issues thoroughly though it had to be recognised that they were given insufficient time to complete their remit.

In discussion it was argued that growth in borrowings or in total liabilities did not itself indicate weakness or otherwise of the business. If sales were increasing the total owed to creditors would necessarily rise. In relation to turnover both the total covered by the Varley-Marshall assurances and the amount owed to creditors were projected to fall significantly between 1985 and 1989. It was not possible to place a limit on the total liabilities subject to the assurances. This was not a total which was computed continuously and lenders or creditors to the company would therefore be unable to establish whether additional credit extended would benefit from the assurances. The company would be unable to trade on this basis. If BL had been operated as a public corporation the limit on its EFL would apply to borrowing not to total liabilities including creditors.

On engines, the Secretary of State for Trade and Industry said BL required a one litre engine to drive the replacement for the Metro. The existing A series engines could not be adapted to meet future emission standards. The company did not believe that an alternative engine could be acquired from outside the company. They therefore proposed to develop their own K series engines.

Summing up this part of the discussion the Prime Minister said that the issue of whether an alternative engine could be acquired should be resolved as soon as possible. Honda should be asked whether they were willing and able to supply an engine which would be suitable for the Metro replacement. A letter should be sent from BL but Ministers would want to approve the text and to see the reply from Honda. If an alternative engine, to be manufactured in Britain, could be supplied it would be preferable to buy it rather than for BL to invest considerable sums to develop its own engine.

The Secretary of State for Trade and Industry set out proposals for collaboration with Honda. These involved joint development and manufacture of a model to replace the Maestro and the Rover 200: manufacture by ARG on a sub-contract basis of Honda models; and construction by Honda of a new engine plant at Swindon which would supply engines for the new collaborative car, the Rover 213 and the cars built under sub-contract for Honda by ARG.

It was argued that extensive collaboration with Honda along these lines was beneficial for BL and was preferable to the development of a greenfield site by Honda. Not only

would such collaboration increase ARG's business but association with Honda, which had a high reputation for quality, would improve ARG's market standing.

Summing up this part of the discussion, the Prime Minister said that collaboration as proposed in the Memorandum of Understanding should go ahead but that ARG's stipulation about the engines it would acquire from Honda would need to be reconsidered when further information was available on the possibility of acquiring an alternative small engine.

The Secretary of State for Trade and Industry recommended that a cap should be set on BL's borrowings and that this should be set at £680 million, the figure to be adjusted to take account of future privatisations. In discussion it was suggested that this figure could be lower; £680 million did no more than accommodate the substantial rise in borrowing projected for 1985. If, however, the figure was set at £680 million and held constant in cash terms to the end of 1987 a progressive squeeze on the company would be achieved. This was agreed.

The Secretary of State for Trade and Industry reported on the prospects for Land Rover-Leyland and for privatisation of Unipart. It was agreed that the BL Board should be pressed to bring forward early proposals including an expected timetable.

Summing up the discussion, the Prime Minister said that the BL Corporate Plan in respect of the Austin Rover group was approved subject to the resolution of the outstanding issue of buying in an alternative to the K series engines. Immediate steps should be taken to establish with Honda whether they were willing and able to supply an alternative engine which could power the Metro replacement and meet forthcoming emission standards. The text of the letter to Honda should be cleared with those Ministers attending the meeting. If it were established that an alternative engine could be acquired from Honda, BL's plans to manufacture its own engines should be revised and the capital expenditure projected under the Corporate Plan scaled down. The broad outline of the collaboration proposals set out in the Memorandum of Understanding with Honda were approved though the statement on the engines which ARG would accept would need to be amended in the light of whatever was decided on the buying in of a small engine. A cap of £680 million should be set on BL's borrowings. This should run until the end of 1987 but be adjusted to take account of further privatisation. The BL Board should be invited to bring forward as soon as possible details, including the expected timetable, for privatisation of Unipart and proposals on Land Rover-Leyland Limited.

SECRET

- 4 -

I am copying this letter to Private Secretaries to members of E(A) and Richard Hatfield (Cabinet Office).

Yours sincerely
Andrew Turnbull

(Andrew Turnbull)

John Mogg, Esq.,
Department of Trade and Industry.

SECRET