



10 DOWNING STREET

SUBJECT  
cc master

file R/S  
a/r Ledwood

*From the Private Secretary*

10 June 1985

*Dear John,*

BL/HONDA

Your Secretary of State came to see the Prime Minister this afternoon to report on negotiations between BL and Honda. The meeting had before it the letter from the President of Honda, which was sent under cover of your letter to me of 10 June.

Your Secretary of State said Honda had reacted to BL's letter about the supply of small engines with a mixture of puzzlement and concern. Mr. Kume's letter made it clear that Honda were not prepared to develop engines jointly or allow ARG to manufacture Honda engines under licence, which they regarded as equivalent to collaboration. Although they had not brought themselves to giving a categorical refusal it was clear that Honda did not want to supply engines for the Metro replacement from Swindon on the grounds that this would greatly increase their commitment to investment and could impair the separate identities of the two companies. Honda were issuing a denial of the report in the Times of 10 June which claimed they were prepared to supply small engines. There were also signs that Honda were backing away from certain aspects of the collaboration agreement. In the Memorandum of Understanding which was supposed to be signed on Friday, they were proposing that references to the engine plant at Swindon should be to a "possible" engine plant.

The Prime Minister thought it strange that Honda should react to an opportunity for more business by threatening to withdraw from the degree of collaboration that they were previously prepared to contemplate. She noted, however, that a lower degree of collaboration might leave HMG with greater freedom should it decide to sell ARG.

Your Secretary of State thought that Honda's reaction could be explained by a fear that the company were being sucked into the problems of BL. The Swindon project would have to be several times bigger than originally planned if it were to supply the engine for the Metro replacement. Having made this substantial investment, Honda might be afraid that a future Government might withdraw support from BL, leaving Honda either stranded with its larger engine plant or forced to help BL financially. This fear had allowed more conservative elements in the Honda organisation to call for a re-appraisal of the whole scheme.

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The Prime Minister said that without a firm commitment to an engine facility, the collaboration deal would be pointless. There could be no question of allowing Honda to import engines for cars being assembled by ARG. Such cars would not satisfy the requirements about domestic content and would therefore be classed as imports and be offset against Honda's quota. This should be made clear to Honda.

Summing up the discussion, the Prime Minister said it was Honda's commercial decision not to extend its involvement with, and dependence on, BL by supplying small engines. The Memorandum of Understanding should not, however, be drafted in a way which closed off the option of acquiring engines from Honda should the company be prepared to expand its commitment to Swindon at some future date. It should also be made clear, either by amending the text or by a side letter, that paragraph 1.7(a) of the MOU referred to accepting Honda engines in existing ARG models. Honda should be pressed to go ahead with collaboration on the basis previously envisaged; but if they wished to refer to a "possible" engine facility, it should be made very clear that the resulting cars assembled by ARG would not be classified as domestically produced. The BL Board should complete its consideration of the Corporate Plan and should signify its acceptance on the EFL agreed at the earlier meeting of Ministers. In the absence of an agreement with Honda for the acquisition of small engines, BL should continue to develop its own K engine. Your Secretary of State was invited to examine the options for selling off ARG with a dowry, with the Varley/Marshal assurances being brought to an end.

I am copying this letter to Rachel Lomax (H.M. Treasury), Leigh Lewis (Office of the Minister Without Portfolio) and Richard Hatfield (Cabinet Office).

*Yours sincerely*  
*Andrew Turnbull*

ANDREW TURNBULL

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

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