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PRIME MINISTER

BL: GM

The note from Morgan Guarantee shows that GM have made a major shift in their position. There are of course several points where further discussion will be needed. But they have gone a long way towards meeting the criteria.

At this stage, you may however like to have a few comments on the timetable for the next few days, to think about overnight.

Unless you disagree, I shall set up a meeting of the inner group for early tomorrow, probably 1045, inviting the Lord President, the Chancellor of the Duchy of Lancaster, Mr. Ridley, Mr. Channon and the Chancellor.

This group will need to decide first whether the latest proposals offer a potentially acceptable deal and secondly whether the next step should be further private discussions with GM or a meeting of MISC 126.

The timetable for further discussion with GM is constrained by the quasi-deadline of 15 April which has been set for the submission of revised bids to BL. It would also be potentially difficult if GM submitted a bid to BL without a wider group of colleagues knowing they would be doing so, particularly if it became known that there had been discussions between Mr. Channon and GM in advance.

These arguments seem to point on balance towards a meeting of MISC 126 tomorrow afternoon, provided the smaller group tomorrow morning judges that the deal now on offer can be pushed through, subject to certain largely second-order changes. (I have asked DTI to prepare a draft paper for MISC 126 which Mr. Channon can bring with him tomorrow morning.)

One outcome of MISC 126 would be approval subject to certain changes. These could be discussed with GM late tomorrow afternoon so that they could put in their bid to BL on Tuesday.

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A complication here is that DTI believe that Mr. Roger Smith, Chairman of GM, will want to speak to you personally before they put in their bid, in order to be assured that success will not again be snatched away from them at the last minute. It may well not be possible to go so firm on assurance, and in any case it may also be undesirable for you to speak to Mr. Smith. But it should be possible to get around this.

If MISC 126 meets tomorrow afternoon the story is very likely to be on the news tomorrow evening. There would be a case for Cabinet to meet on Tuesday morning to hear a report and, in effect, to take note of GM's wish to make a further bid and MISC 126's agreement that they should be allowed to do so. Cabinet would also need to meet if Mr. Walker and Mr. Fowler refused to go along with the proposal to countenance a bid from GM. (Neither MISC 126 nor Cabinet could decide to accept a bid from GM even in principle: the deadline for receipt of further bids would not have passed, nor at that stage would the Government have received the benefit of the advice of the BL board.)

The BL board is likely to meet on Tuesday night or Wednesday morning. Particularly if GM are in the field, it would be best if Cabinet took the decision on Thursday morning, possibly following a meeting of MISC 126.

This timetable would allow a statement on Thursday afternoon. There would also probably be pressure for a statement on Tuesday and Wednesday if GM's interest becomes known tomorrow.

Amanda Rose

DP DAVID NORGROVE
13 April 1986

SLH/72

SECRET

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David Norgrove
No 10.

Attached Morgan Guaranty letter
is still subject to some clarification
and amendment especially on the
key aspect of when HM's Golden
Share ~~after~~ would expire.

Richard Brown

DTI

CCB/UP

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Dear Mr Brown,

As you are aware, the Morgan Bank acted as financial advisor to General Motors Corporation in the latter's recent negotiations for the purchase of the Land Rover-Leyland business of BL plc.

Since the termination of those negotiations on March 21 1986, the Morgan Bank has been attempting to develop internally a structure for the transaction which would meet the legitimate objectives of General Motors Corporation, Her Majesty's Government and BL plc. The purpose of this letter is to outline to you a structure which appears to secure the objectives of each party while providing adequate protection for the interests of both sides.

The Morgan Bank believes that an acquisition of Land Rover-Leyland based on the principles outlined below would represent an acceptable solution to General Motors Corporation. However, it is in our judgement unlikely that the company would be willing to submit a revised proposal incorporating this structure unless it receives appropriate assurances as to the ultimate likelihood of such a proposal proving acceptable to Her Majesty's Government.

The structure developed by the Morgan Bank is composed of the following major elements:

- o General Motors Corporation ("GM") will own 100% of Land Rover-Leyland excluding the Land Rover four-wheel drive business (but including LRPE).
- o GM will own 49% of the Land Rover four-wheel drive business, consisting of the operations currently managed by Land Rover Limited.
- o GM will handle all sales and distribution of Land Rover products outside the United Kingdom.

- o The balance of the Land Rover four-wheel drive business will be owned by a group of 10-20 UK institutions, whose shares will be held on the following basis:
 - the shares will initially be unlisted but a flotation of the institutional shareholdings will be expected to take place within three to five years
 - restrictions on the accumulation of shares will apply so that no individual shareholder other than GM will be able to control more than 5% of the voting rights of the outstanding stock; GM will be restricted to 49% of the voting rights under the terms of a golden share held by Her Majesty's Government
 - GM would have the right of first refusal over the economic interest in Land Rover represented by any shares offered for sale by the institutional investors
 - with the above exceptions, there would be no constraints on the transferability of the institutions' shares in Land Rover.

- o Board representation will be proportional to the voting rights attached to shareholdings.

- o The extinction of the golden share held by Her Majesty's Government would be triggered by flotation, a reduction below five in the number of investors other than GM holding shares in Land Rover, or the attainment of specified levels of unit production at Land Rover.

- o Implementation of this structure will take place in three stages:
 - Purchase by GM of the entire Land-Rover Leyland Group
 - Transfer of the assets of the Land Rover four-wheel drive business to a new company
 - Offer of shares in the new company to UK institutions.

As you will recognise, this structure has some significant disadvantages for General Motors Corporation in relation to the transaction originally envisaged. In particular, General Motors Corporation will forfeit control of the Land Rover four-wheel drive business and will surrender its flexibility to achieve optimal funding for the entire Land Rover-Leyland group.

£134m

The new structure therefore implies a diminution in value for the Land Rover-Leyland group as a whole, and the value of the transaction on the revised basis is unlikely to exceed £180 million.

Of this amount, approximately £160 million is attributable to the Land Rover four-wheel drive business, which, when constituted as a separately incorporated entity, will be capitalised with £90 million in equity and £70 million in debt. The placement of 51% will therefore be intended to raise £46 million from the UK institutions (i.e. 51% of £90 million).

In the absence of the opportunity to pre-sell the shares to the institutions prior to the acquisition of Land Rover-Leyland, there is inevitably an element of uncertainty surrounding the proceeds of the anticipated placement, and General Motors Corporation will not be in a position to guarantee that the total value realised by BL plc (composed of a cash payment by General Motors Corporation of £134 million plus the proceeds of the placement up to £46 million) will in fact amount to £180 million. Any surplus on the proceeds of the placement over £46 million would mutually benefit BL plc and General Motors Corporation.

General Motors Corporation may be willing to contemplate the assumption of underwriting risk if that incremental risk were reflected in an appropriate reduction in its own cash payment.

If you believe that the transaction outlined in this letter has the potential to meet the objectives of Her Majesty's Government, the Morgan Bank would be happy to explore the structure with you in more detail at your convenience.

Yours sincerely,

pp Alfred M. Vinton, Jr.

Flotation

100%

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