

SECRET

21



Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

cebg

PRIME MINISTER

Prime Minister²
no

DLW
1/9.

ROVER GROUP

at flap

I have seen Paul Channon's recent minute to you about Rover Group and your comments (recorded in your Private Secretary's letter of 9 September).

It hardly needs stressing that Graham Day's recommendations on the future of the Group are likely to raise major issues, including important implications for public expenditure. I therefore think it is essential that we should be fully informed about all the options in good time. Day will no doubt wish to put forward his preferred option but we must know what other options Rover have considered, the arguments that support them, and the Board's reasons for discarding them. The sooner that Paul can give us indications about the possible public expenditure consequences of the deteriorating trading position of the Group and of the potential for disposals, the better.

On the sale of Istel, while I understand the case for Rover Group retaining a minority stake sufficient to allow representation on the Board, I am not convinced that this stake needs to be as high as 25%; 10% may be sufficient, particularly if there is an arms length supply contract between Rover Group and Istel.

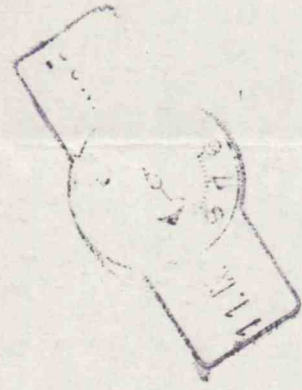
I am copying this minute to Paul Channon.

N.L.

N.L.

9 SEPTEMBER 1986

Ind - POL - BL PT12



INDONESIA

CONFIDENTIAL

MJ2 C17



oB6

10 DOWNING STREET

LONDON SW1A 2AA

From the Private Secretary

9 September 1986

ROVER GROUP

The Prime Minister was grateful for the report on the present situation of the Rover Group set out in your Secretary of State's minute (undated).

The only point for immediate decision appears to be whether RG should continue to hold a minority stake in ISTEEL after it is sold. The Prime Minister is content, subject to the Chancellor's views, that RG should hold a 25 per cent minority stake.

I am copying this letter to Tony Kuczys (HM Treasury).

David Norgrove

Miss Catherine Bradley
Department of Trade and Industry.

CONFIDENTIAL

dg

CONFIDENTIAL

PRIME MINISTER

ROVER GROUP: ISTEEL

Yes / ref

Could I ask you to confirm please that you are content *
for Rover Group to retain a 25 per cent stake in Isteel when
it is sold? (See paragraph 3 of Peter Warry's minute and
paragraphs 5 and 6 of Mr. Channon's minute. A 25 per cent
stake might be worth around £10 million. There is, however,
a suggestion that the value of the company as a whole might
be reduced if Rover Group were to retain no stake at all, on
the grounds that Rover Group are very important customers and
the financial connection helps to tie in the business.)

DKN

David Norgrove

A subject to the Chancellor's views

8 September 1986

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PRIME MINISTER

4 September 1986

ROVER GROUP

1. Management Changes

Harold Musgrove's departure must be good news but I doubt if it will be as quiet as Graham Day hopes. His successor, Les Wharton, is a solid professional manager who will run the business in a responsible and non-political manner. As Managing Director of Leyland Trucks he was seemingly the sole BL manager to circulate to his employees explaining why the GM bid was the right way to go.

2. Austin Rover and Honda

With new management there is no doubt that Austin Rover's dreadful performance can be improved, but the relationship with Honda will still remain a critical consideration. It is reassuring that Honda have not been prepared to take an immediate equity stake as it hopefully shows that they are treating it as more than a matter of window dressing.

3. Sale of ISTEEL

ISTEEL is crucial to Austin Rover's performance as its data processing and CAD/CAM system lies right at the heart of ARG's business. Graham Day is being quite brave in selling 75% of the business and it is surely right that Rover should retain the other 25%. There is little money or risk for the Government in this residual holding.

4. Bedford Trucks

It is a pity that Graham Day has been unable to salvage anything from Bedford's demise, but presentationally it

SECRET

makes the Government's life easier. The DTI's proposed briefing line seems sensible but it will be worth pressing the Labour Party to explain what they now think of their anti-American policy.

Peter Warr
PETER WARRY

- 2 -

SECRET



010

S E C R E T

cc BGG 20
return please

JU308

PRIME MINISTER

ROVER GROUP

You may care to have a report on the present situation since we last discussed it.

RG PERFORMANCE IN 1986 AND THE OPERATIONAL REVIEW

2 RG's commercial and financial performance this year continues to be disappointing. Austin Rover's performance is a particular cause for concern with UK market share in the key month of August likely to be only about 14%. The half year results will be available shortly and I will report again later this month. Day's broad view is RG's performance is no worse than he anticipated and underlines the need for radical options to be examined and for difficult decisions to be faced when the results of his operational review are to hand. The September RG Board will have a first draft of the review. Day envisages that he will be able to let us have a first look at real options in October. I will keep you closely in touch.



S E C R E T

TRUCKS

3 Serious talks are taking place with DAF on joint production and marketing, moving on to the financial discussions before the end of the year. A full accountants report on Trucks should be available for Paccar by the end of September to enable discussions to go forward in parallel. Day has resisted pressure from DAF for an exclusive negotiation. He hopes to bring both sets of talks to the point where RG can make a recommendation in the first quarter of 1987. Day is clear that DAF cannot be pressed to conclude their own appraisal more quickly. I believe we must accept his view though we shall need to prepare contingency press briefing against possible leaks in the autumn.

4 In my separate minute today I reported to you the situation on Bedford commercial vehicles. RG discussed with Bedford the possibility of securing advantage from their decision to withdraw from truck production in the UK, outlined in my separate minute today. RG have considered carefully whether taking over Bedford's distribution network would have facilitated a subsequent disposal of Leyland Trucks. Such a step would have involved RG paying Bedford to manufacture 2500 trucks until Leyland could develop a Bedford badged Leyland truck to supply the Bedford network. This would have cost RG £10m for continued



S E C R E T

production of Bedford vehicles plus the cost of development of the badged truck and the purchase of the parts business worth some £20m. Leyland Trucks take the view that such a step might raise their market share to 25% from their current market share of 18%, compared to the further 2% of the UK market that they might gain in an open competition for Bedford dealers. However, Day's view is that the benefits are too uncertain. The return on such an investment would only be realised over a period of several years, and the possible incremental value would be viewed as unproved by any potential purchaser of trucks. Both RG and Bedford now regard this proposal as dead.

ISTEL

5 I have also explored Day's views on the disposal of RG's computer services subsidiary, Istel. Day's objective is to seek competitive tenders from among the wide range of companies, including American and French as well as UK ones, who have expressed interest in Istel. Day emphasised, however, that in determining RG's final choice he would wish to consider not only price but also the needs of RG as a user of Istel's services. Day is confident that competitive bids from UK as well as foreign companies can be expected to come forward. Naturally RG must try to secure maximum value for the business. Other things being equal, I would welcome a British solution for this company which has a leading capability in computer integrated manufacturing and




S E C R E T

value added networks. RG must also have regard to their own interest as a user.

6 It is for this reason that Day also feels strongly that RG should continue to hold a 25% minority stake in Istel and to exercise an influence on its commercial policies through the terms of a shareholders' agreement. Currently 50% to 60% of Istel's business is with RG, and ARG's operations are intimately linked to the computer services Istel provides. There are strong parallels to the interrelation between RG and Unipart and in this particular case I am inclined to accept Day's argument. The RG Board will be considering Istel at their Board meeting on 16 September. Subject to the views of colleagues, I should like, therefore, to tell Day that we accept his arguments for a minority shareholding within the next week. RG are anxious to offer tenders to potential bidders in October with a view to disposal by the end of the year.

ARG AND HONDA

7 Exchanges between RG and Honda are continuing. Day believes that Honda are in principle willing to consider taking a significant minority stake in ARG, provided this did not under Japanese accounting conventions require consolidation of ARG results into Honda's accounts. This is thought to indicate a holding of something less than 20%. But Day believes it unlikely





S E C R E T

that Honda would come in until such time as ARG shows a cleaner picture on reliability of its products, marketing strategy and financial performance. In the meantime Day intends to continue to seek to reinforce the manufacturing links with Honda.

UNIPART AND LEYLAND BUS

8 Following our Parliamentary announcement of the decision in principle to sell Leyland Bus and Unipart on 24 July contract negotiations are moving forward satisfactorily though a range of complex issues remain to be cleared in both companies. It is hoped that contract negotiations may be concluded in October. I have indicated that we would wish to see both deals completed at the earliest possible date.

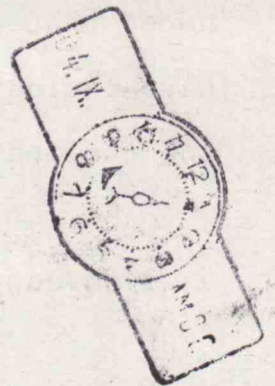
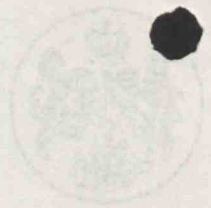
9 I am copying this to Nigel Lawson.

A handwritten signature in blue ink, consisting of the letters 'P' and 'C' joined together.

PAUL CHANNON

September 1986

Department of Trade & Industry





DEPARTMENT OF TRADE AND INDUSTRY
1-19 VICTORIA STREET
LONDON SW1H 0ET

Telephone (Direct dialling) 01-215) 5422
GTN 215)
(Switchboard) 01-215 7877

Secretary of State for Trade and Industry

**CONFIDENTIAL
COMMERCIAL IN CONFIDENCE**

9 October 1986

The Rt Hon Nigel Lawson MP
Chancellor of the Exchequer
Treasury Chambers
Parliament Street
London
SW1P 3AG

Nigel

NBSM

ROVER GROUP/ISTEL

at top
In your letter of 9th September you queried the size of the stake the Rover Group proposed to retain in Istel. I had the chance to revert to Graham Day on this matter during a recent meeting and I found him particularly emphatic about the Board's view that 25% was the appropriate shareholding. Your officials have had sight of the further letter from the company on this matter in which they set out their reasoning.

The fundamental point RG stress is the mutual inter-dependence of Austin Rover and Istel. Retention of a significant stake would therefore be interpreted by a potential purchaser as an important sign of continuing commitment to Istel; reducing that stake could affect the overall valuation of the company. Like you I am concerned that RG should not, especially in current circumstances, fail to take full advantage of any practical opportunities to generate funds; however I can understand why they do not believe in this instance that increasing the size of the stake to be disposed of will simply give a pro rata increase in the sum realised.

The other factor RG are concerned about is protecting their own interests after the disposal. They see the retained stake, the Austin Rover/Istel supply contract, Istel Board representation and other rights (e.g. on pre-emption) secured by the shareholders agreement as a single package to this end. There must be some

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BOARD OF TRADE
BICENTENARY



doubt as to whether it would prove possible to negotiate a satisfactory shareholders agreement for a significantly smaller stake.

I know that RG are particularly encouraged by the expressions of interest they have had in Istel and keen to proceed quickly with negotiations. Given the background of more difficult issues over the Rover Group I hope you will now agree that this is not an issue we should seek to press the Board against its own judgement and that of their advisers.

I am copying this letter to the Prime Minister.

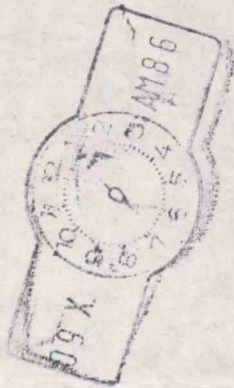
A handwritten signature in black ink, appearing to be 'Paul', written over a large, stylized 'X' mark.

PAUL CHANNON

A handwritten signature in black ink that reads 'Paul', written in a cursive style.

JSLAKI

INDPOL BL P712





Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

13 October 1986

Miss Catherine Bradley
Private Secretary to the
Secretary of State for Trade and Industry

Dear Catherine,

NBN

ROVER GROUP/ISTEL

The Chancellor was grateful for your Secretary of State's letter of 9 October, about the size of the stake that Rover Group wish to retain in Istel.

The Chancellor remains sceptical about the arguments advanced by Rover Group for the need to retain a 25 per cent stake in Istel. Nor has any hard evidence been produced that a minority holding significantly lower than this would have a material impact on the likely sale price. However, at the end of the day this is a matter of commercial judgement for Graham Day and his Board. If DTI are fully satisfied that their arguments for foregoing sale receipts of perhaps £6 million are well founded, the Chancellor does not want to press the issue.

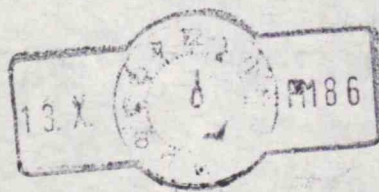
I am copying this letter to David Norgrove (No.10).

*Yours sincerely,
Cathy Rydin*

AP

A W KUCZYS
Private Secretary

IND POC : BL PT12





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COMMERCIAL IN CONFIDENCE

CCBG

JU306

cc BT and
reborn

PRIME MINISTER

BEDFORD TRUCKS

You should be aware that Bedford Commercial Vehicles, under pressure from their GM parent to stem losses which reached £73m in 1985, have decided to withdraw from civil truck production in the UK at Dunstable. An announcement will be made within the next ten days and I will keep you in touch on exact timing. I have discussed the position with GM and Bedford senior management and it is clear that the decision is final.

2 Bedford will be announcing that their military truck operations and spares operations, also based at Dunstable, will continue as going concerns; although I understand that they may be sold within the next six months to an as yet unspecified purchaser. The Dunstable plant will continue for the present on that basis. However, the long term future of the military business, under Bedford or other management, is likely to depend on MOD's procurement decision on a new general purpose truck for



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introduction at the end of the decade. Bedford are competing with Leyland and Volvo. A decision is expected in 1988. My officials are in contact with MOD on this.

3 At the beginning of 1986 Bedford employed 7000 people in total, with 2300 in trucks at Dunstable and 4600 in vans at Luton. Bedford will continue their van operations but a programme of 1700 voluntary redundancies spread across trucks and vans announced in June this year is now likely to be followed by substantial further redundancies as a result of the withdrawal from civil truck production and a further review of staffing levels. Bedford have indicated that this could be as high as two thousand, which they hope can be effected on a voluntary basis. The initial 1700 voluntary redundancies were oversubscribed.

4 I expect that there will be strong competition for Bedford's distributors and 9% share of the UK market. Rover Group expect to pick up some 2% of the market, but a substantial proportion will undoubtedly fall to importers, led by Mercedes.

5 The possibility of such a decision has already been leaked by GM management in the United States. However, Bedford management have underlined to me the need to avoid any further disclosures until a formal statement can be made to the workforce.



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6 I am copying this minute to members of MISC 126, to the Secretaries of State for Defence and Employment, and to Sir Robert Armstrong.

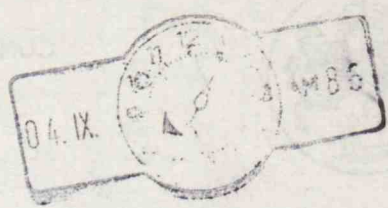
PC

PAUL CHANNON

September 1986

Department of Trade & Industry

COMPLIANCE
GENERAL IN COMPLIANCE



GENERAL

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COMMERCIAL IN CONFIDENCE

cc/BG



DEPARTMENT OF TRADE AND INDUSTRY
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JU310
PS (Secretary of State for Trade and Industry)

3 September 1986

David Norgrove Esq
Private Secretary to the
Prime Minister
10 Downing Street
London SW1

cc/BG and return.

This announcement is to
be made tomorrow morning,
9/9.

Dear David

JW
8/9.

BEDFORD COMMERCIAL VEHICLES

... As promised, I attach a line to take on the decision by GM to withdraw from civilian truck production at Bedford. We will update it as the timing and the detailed implications of the decision are clearer. Meanwhile, in advance of a statement from Bedford, we will not comment on any speculative reports.

Yours

Timothy Walker

TIMOTHY WALKER
Private Secretary

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19 **86**
BOARD OF TRADE
BICENTENARY

COMMERCIAL IN CONFIDENCE

BEDFORD COMMERCIAL VEHICLES

WITHDRAWAL FROM (CIVILIAN) TRUCK PRODUCTION

LINE TO TAKE

In advance of statement by Bedford

No comment. Commercial operation of their plants entirely a matter for Bedford.

Following an announcement by Bedford (expected between

8-15 September)

A matter for Bedford.

For Bedford, as for any other commercial company, it is for the management to determine how to respond to market conditions.

Government regrets but understands the decision which Bedford has considered it necessary to take, against a background of very difficult competitive conditions.

COMMERCIAL IN CONFIDENCE

Q Decision the Government's fault?

Q Direct result of mishandling the GM/RG talks?

The Government has stated on many occasions that it regretted the ending of RG's discussions with GM. Unfortunately GM was not able to give the assurances which the Government considered to be necessary on the future of Land Rover, and GM declined to carry forward talks solely on Trucks.

As the Government made plain at that time, fundamental problems of over-capacity in the commercial vehicle sector remain.

It is against that background that Bedford have taken their decision to discontinue civil truck manufacture at Dunstable.

Sure that Bedford examined all options fully before reaching this considered decision, based on commercial realities.

Q What about Leyland Trucks? Are they to be protected by the Government's shareholding while Bedford goes to the wall?

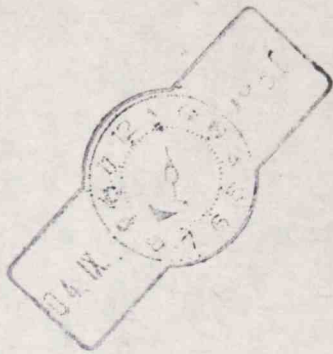
Substantial rationalisation and job losses have taken place in Leyland Trucks, as in other parts of the commercial vehicle industry. At the end of the day, all companies, whether in public or private ownership, have to face the challenge of market conditions.

COMMERCIAL IN CONFIDENCE

BACKGROUND

1 Bedford Commercial Vehicles are expected to announce in the week beginning 8 September a decision to withdraw from the manufacture of civil trucks in the UK at Dunstable. Production of military trucks and spare parts will continue at Dunstable, while production of vans will continue at Luton.

2 Bedford Commercial Vehicles employ 7000 people in total, 2300 at Dunstable on trucks and 4600 at Luton on vans. Withdrawal from the production of civil trucks, together with a further general review of staffing level is expected to result in a substantial programme of further redundancies, following the announcement in June 1986 of plans for 1700 voluntary redundancies at Dunstable and Luton. It is hoped that this further round of redundancies can also be effected on a voluntary basis.





ECL

10 DOWNING STREET
LONDON SW1A 2AA

From the Private Secretary

30 September 1986

GF
Do you wish to
keep?
D/110

Thank you for your letter to the Prime Minister of 29 September. I am sure she will be grateful for the information about your negotiations with DAF.

(David Norgrove)

J. Graham Day, Esq.

BM.

Prime Minister²
For letter from
Graham Day attached.

MR NORGROVE

DAN

30 September 1986

3/9.

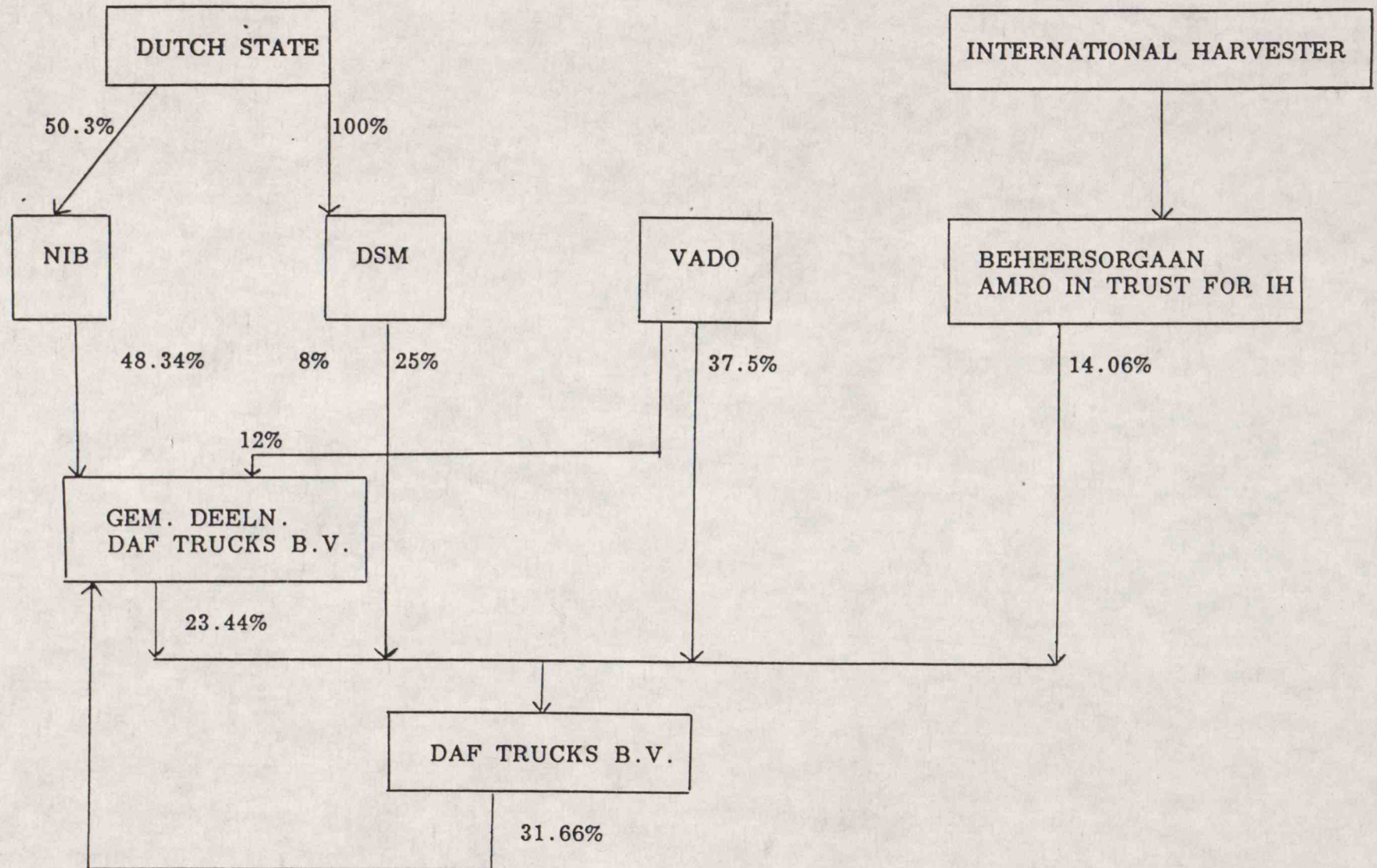
DAF TRUCKS

The attached chart shows the various shareholdings in DAF Trucks. The Dutch State own 25% of the company ~~directly~~ and it has a share in an intermediary company which in turn owns 23% of the business. DAF is therefore not either a state-owned or a state-controlled company

Peter Warry

PETER WARRY

DAF TRUCKS



29 September 1986

The Rover Group plc
7-10 Hobart Place
London SW1W 0HH
Telephone: 01-235 4311
Telex: 926880

Rt. Hon. Margaret Thatcher, MP,
Prime Minister,
10 Downing Street,
London SW1

R30

COMMERCIAL IN CONFIDENCE

Dear Prime Minister

Mr. A. van der Padt, the Chairman of DAF Trucks, has told me that tomorrow he will be briefing the Dutch Prime Minister on current and prospective relationships with Leyland Trucks and Freight Rover. Consequently, I thought it would be helpful for me to bring you up-to-date so that you can respond as you see fit in any exchanges, casual or otherwise, with the Dutch Prime Minister.

As I advised you when we last met, the Dutch Government shareholding in DAF is held indirectly and, thus, DAF does not have contact with its Government of the nature and to the extent which we do. Van der Padt's view is that the current commercial arrangements with Leyland Trucks and Freight Rover, together with the possibility of a future more fundamental relationship, are of such importance that his Government should be aware.

On the commercial front, on Friday I signed agreements whereby Freight Rover will provide DAF with medium and heavy commercial vans, bearing the DAF badge, for sale through DAF dealers in Europe. Similarly, Road Runner trucks will be provided by Leyland Trucks. Both agreements are supplemented by Parts and Supply contracts. These arrangements apply until cancelled by either party on five years notice.

On the van side, the minimum volumes over the initial 5 years range between 900 and 1500. For planning purposes we believe that towards the end of the initial 5 year term the actual numbers will double or more. Comparable numbers for trucks range between 550 and 1200.

Directors:
J. Graham Day (Chairman and Chief Executive)
Sir Robert Hunt CBE DL (Deputy Chairman)
Sir Robert Clark DSC
Sir John Mayhew-Sanders
B. W. Pomeroy

Registered Office:
7-10 Hobart Place
London SW1H 0HH
Registered in England No 1213133

COMMERCIAL IN CONFIDENCE

- 2 -

This is important business which will contribute between 5 - 10% volume improvement; Freight Rover's profits will be increased and Truck's losses will be contained in part.

DAF, through securing vans and medium trucks from us, are thus able to offer a full range of products, matched in Europe only by Mercedes and Ford Iveco.

As you know, one of the alternatives for the disposal of Trucks involves DAF. As contrasted with the American alternative, Paccar, it is increasingly clear that the DAF solution would include Freight Rover also. With DAF we have set up a number of Working Parties who will report at the turn of the year. Given that the result of this is positive overall, a proposal will be developed which can then be set against other disposal alternatives.

Privately, DAF tell me that their thinking in structural terms would be to create a fresh company which internally they describe as the "Anglo Dutch Joint Venture". This company would hold all of the DAF shares plus Leyland Trucks and Freight Rover. Should this occur, DAF's planning intention would be to float the joint business on the Amsterdam and London Stock Exchanges towards the end of 1988/early 1989.

If there is any additional information which you may require please ask your office to contact me. I hope that the foregoing will enable you to deal effectively with any casual exchange which may arise with the Dutch Prime Minister.

Sincerely
Baker

J. GRAHAM DAY

cc: Rt. Hon. Paul Channon, MP
Mr. Giles Shaw, MP