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The paper for the
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PRIME MINISTER

ROVER GROUP (RG): LEYLAND TRUCK AND BUS

We need to consider the position which has been reached on the privatisation of Leyland Bus and of Leyland Trucks and the financial issues related to those sales.

LEYLAND BUS

Detailed negotiations between RG and the proposed management buy-out team are at an advanced stage and it will be clear very soon whether all the outstanding questions can be successfully resolved. Cash receipts would be negligible, but we should have released the tax-payer from supporting this severely loss-making business.

LEYLAND TRUCKS

There are two disposal options:-

- (i) Paccar (Foden) have confirmed their intention to put in firm proposals in December. Their interest is confined to Trucks. If Paccar do bid, Cummins engines may support them with an equity participation. The UK independent truck manufacturer, ERF, might also be involved.
- (ii) DAF are interested in Freight Rover as well as Trucks. A combined DAF/Leyland Trucks/Freight Rover company would probably be formed as an interim step before flotation in 2-3 years time. Until flotation, Rover Group would retain a 25-30% share of the equity in the joint company. DAF's decision in principle is also expected in December.

Graham Day expects to recommend at the end of the year which Trucks option he wishes to pursue with a view to reaching Heads of Agreement by February. In case neither of these potential deals should materialise, he is preparing a fall-back restructuring plan for Trucks under present ownership.

Under either of the sale options - or retention within Rover Group - substantial rationalisation of facilities (list at Annex A) would be needed and serious job losses would be unavoidable. The scope, location and timing of these cannot be identified at this stage but:



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- DAF would retain the Leyland assembly plant, though with reduced manning, and the Freight Rover operation in Birmingham where it would also fund new model development. The future of the Scammell plant at Watford and the Albion axle plant in Glasgow would be reviewed but these facilities would not necessarily be closed.
- Paccar would reduce the Leyland operations to the assembly-only of vehicles from bought-in components. Peripheral activities including Scammell, Albion and engine/foundry production at Leyland would almost certainly be closed as well as (if ERF were involved) either the ERF or Foden plants at Sandbach. There would be further consequential job losses in component supplier companies arising from UK rationalisation and some overseas sourcing.
- Under the Rover Group 'retention option' restructuring within Leyland Trucks would be likely to follow closely the Paccar pattern.

Under the DAF proposals, at least 2000 jobs would probably need to go within Leyland Trucks. With the Paccar or RG 'retention' options perhaps as many jobs again would be at risk as retrenchment within Leyland would be more severe and the impact on the components sector might also be significant.

The political and industrial drawbacks of the Paccar proposals would be substantial. Whilst for the moment Graham Day must clearly pursue both disposal options, Paul Channon and I take the view that he should be asked to give priority to DAF even though this would require Rover Group temporarily to retain a minority holding in the proposed new joint company. The extent, if any, to which Rover Group under the DAF option would continue to have some financial obligation to this new company is unclear (though Graham Day will be asked to negotiate to minimise this risk). However the Government's commitments under Varley-Marshall assurances - currently around £450m in respect of Trucks and Freight Rover - would obviously be terminated.

FUNDING - RESIDUAL DEBT OF BUS AND TRUCKS

On the assumption we are successful in disposing of Trucks and Bus, we need urgently to decide how to tackle the large historical debts in these companies and the restructuring



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costs which the potential purchasers will insist should be for RG's account. The combined Bus and Trucks debt plus restructuring costs is estimated at around £650m but a number of uncertainties surround this figure related to how quickly the deals go through, the range of businesses ultimately covered and the precise terms negotiated between the various parties.

We agreed on 1 July that we would need to provide funding to prevent this legacy falling on the residual Group, so the question is - over what timescale should we act? Taking into account the Chancellor's concerns about avoiding public expenditure costs in 1987/88, Paul Channon has agreed with him that the right course would be to fund the write-off of debt and restructuring costs in 1986/87. This is also the course which makes the best commercial sense for Rover Group. If we were to fail to act quickly and with conviction, the credibility of the Group and in particular of Austin Rover and their products would decline further. Graham Day believes there would be a real risk in these circumstances that customer and dealer confidence would collapse.

To achieve this timetable urgent clearance of this funding by the EC Commission will be required. Commissioner Sutherland has told me that, while the Bus write-off should not present too many difficulties, he would be under the strongest pressure to open formal procedures to investigate any deal on Trucks. We may need to apply pressure of our own to push this through by March 1987. Meanwhile I propose that officials should move quickly to tell the Commission in the strictest confidence what we intend to do. The Commission will need to know the parties involved, the restructuring envisaged and the potential impact of any deal on the European truck industry. A deal with DAF however is likely in principle to be more acceptable to the Commission because it would secure a European rationalisation.

PRESENTATION OF GOVERNMENT POLICY

Public presentation of decisions on RG requires careful thought. We must show that we have a clear plan and we must retain the initiative.

If the Bus talks are successful it may be possible to announce further progress on these next month. In any case we must recognise that some statement on Trucks will be required before any deal is finalised. Speculation about DAF and Paccar is building up in industry circles and, as



with GM and Ford, we are again in danger of being confronted in the House with charges of more "secret" talks. To avoid our being caught on the back foot, Paul strongly favours a pre-emptive statement as early as possible in December which would:

- underline the difficult conditions still confronting truck manufacturers and the need for collaboration in order to survive;
- acknowledge that Rover Group are talking to DAF and Paccar and indicate Government support for these talks;
- promise a full statement when the outcome of these talks is known.

In any pre-emptive statement, we should need to be very guarded about what we say on the treatment of debt. We should therefore need to deflect questions by reference to the forthcoming 1987 Corporate Plan which would address the overall financial situation of Rover Group.

Beyond the very short-term, we need to prepare for a positive and comprehensive statement in February covering:-

- agreement on disposal of Leyland Trucks to either DAF or Paccar;
- Government funding of the order of £650 to enable the write-off of historical debt;
- the Government's response to the 1987 Corporate Plan, in substance the strategy for Austin Rover.

The timing of this latter statement would coincide with Rover Group's need to announce an Extraordinary General Meeting to relax the borrowing restrictions in its Articles of Association; and the requirement on the RG Board and auditors to comment formally on the adequacy of the Group's working capital in a circular to shareholders related the sale of Leyland Bus. On their own these might attract (unfavourable) media comment. Alongside a positive Government statement, they would have little news value.



Frederick Rover

RECOMMENDATIONS

I recommend:

- (a) that Graham Day be asked to pursue both disposal options for Leyland Trucks, but to give priority to DAF with the objective of reaching Heads of Agreement by February;
- (b) that officials should be asked to discuss urgently with the EC Commission in the strictest confidence, how best to obtain their authorisation to write-off the Bus and Truck debt in 1986/87.
- (c) that we plan to make a pre-emptive announcement about Bus and the talks on Leyland Trucks with DAF and Paccar as early as possible in December;
- (d) that we plan to make a substantive, comprehensive statement on Rover Group in February.

I am copying this letter to Willie Whitelaw, Nigel Lawson, Norman Tebbit, Nicholas Ridley and John Wakeham.

GILES SHAW
26/11/86

COMMERCIAL IN CONFIDENCE

Company	Activity	Employment as at:	No	Rationalisation Plans	
				Closure timing	Redundancies Announced
<u>Leyland Bus</u>					
Workington, Cumbria	1 Bus and coach chassis assembly 2 Rail production	1.5.86	388	-	131 (Aug 86)
Farington, Leyland Lancs	1 Component manufacture 2 Chassis assembly	1.5.86	1296	-	486 (Aug 86)
Eastern Coach Works Lowestoft, Suffolk	Double-deck body manufacture and assembly	1.5.86	484	1987	484 (July 86)
Chorley, Nottingham Bristol, Glasgow	Services Centres	1.5.86	181	-	-
Thurston Rd, Leyland	Head Office	1.5.86	347	transfer	158 (Aug 86)
<u>Leyland Trucks</u>					
Albion, Glasgow	Axle manufacture	30.6.86	1073		
Bathgate, Scotland	1 Assembly 2 Engine manufacture	Sept 86	6	1986	1504 (Complete by Oct 86)
Leyland, Lancs	1 Truck assembly 2 Component manufacture 3 Engine manufacture 4 Foundry	30.6.86	4366		284 (June 86)

ITUCFX

Company	Activity	Employment as at: No		Rationalisation Plans	
				Closure timing	Redundancies Announced
Watford, Herts	Scammell heavy and military trucks	30.6.86	717		126 (Nov '86)
<u>Leyland Parts</u>					
Chorley, Lancs	Parts manufacture and supply for bus and trucks	30.6.86	1278		100 (Nov '86)
<u>Freight Rover</u>					
Birmingham	Vans	Sept 86	1851		
<u>Bedford (GM)</u>					
Dunstable, Beds	Truck manufacture Specialist and military vehicles				
Luton	Vans				
Luton	Central administration and sales staff				
Bedford TOTAL	-	1985	7000	end 86 med/hvy (excl military)	1700 (June 86) 1450 (Sept 86)

ITUCFX

Company	Activity	Employment as at: No		Rationalisation Plans	
				Closure timing	Redundancies Announced

ERF

Sandbach, Cheshire	Assembly of heavy commercial vehicles	1985	1000		
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Foden

Sandbach, Cheshire	Assembly of heavy commercial vehicles	1985	445		
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