

*Subject ce master**file*

10 DOWNING STREET

LONDON SW1A 2AA

*From the Private Secretary*

16 December 1986

*Dear Mike,*ROVER GROUP

The Prime Minister this morning held a meeting to discuss your Secretary of State's minute of 12 December about the Rover Group. There were present your Secretary of State, the Chancellor of the Exchequer, Mr. Giles Shaw (Minister of State, Department of Trade and Industry) and Mr. George Guise, No. 10 Policy Unit.

Your Secretary of State said the negotiations on Leyland Bus were now virtually concluded. An announcement on a management buy-out for ISTEEL might be made this week. The discussions on Leyland Trucks were going well, and the announcement to Parliament seemed to have helped. There was a reasonable prospect that the European Commission would, tomorrow, approve on the nod a debt write-off for Leyland Trucks and Leyland Bus which could be carried out whether a deal was struck with DAF, PACCAR or there was no deal at all. The ARG Corporate Plan was expected by the end of the year. The position of ARG was serious. Its market share was now down to 12.89 per cent.

The meeting then discussed Honda's request for an assurance from the Government that in the event of ARG being taken over by a third party, Honda would be welcome to develop their own assembly operation at Swindon. It was noted that the Government would have no formal powers to prevent such development, though a company like Honda would be unlikely to proceed with it unless it had the Government's backing. It was agreed that Mr. Day should now give the assurance. But it should be placed in the context of the agreement on design and development of the AR8. There need be no formal statement that the assurance would lapse if the agreement did not go ahead. It would be more a matter of saying that Honda had sought the assurance in the context of negotiating the design and development agreement and in that context the Government was happy to give the assurance: if Honda showed faith in Britain, that faith would be reciprocated.



There was a brief discussion of the prospects for ARG and a wider agreement with Honda. Your Secretary of State said the prospects of a Honda equity stake seemed, if anything, less likely than they had earlier. It was noted that there could well be disadvantages to Honda taking an equity stake, from the Government's point of view as well as from Honda's own point of view. It could tend to foreclose options and Honda would have a seat in the Board Room of a potential future competitor. It might be preferable to proceed by way of further joint ventures.

In discussion of the proposed deal between Leyland Trucks and DAF it was noted that whilst Leyland would be taking no debt into the new company, DAF would be carrying in its entire debt. This was asymmetrical and it would also mean a weaker joint company. Rover Group should push for the DAF shareholders to make an equity injection in order to strengthen the joint company, to reduce the likelihood of a call on its shareholders by the joint company and in order to reduce the UK equity stake. (The need to fund investment in new products for Freight Rover - paragraph 9 of Annex C - further strengthened the case for an equity injection.) It was agreed that this should be pursued as an important objective, but not as a condition for a deal. It was further agreed that the negotiations should aim to keep open the option for the Government to place its shares after, say, 1 January 1988, and if possible to secure an understanding that there would be no further calls for capital by the new company. It was noted, however, that further calls for capital could not be ruled out entirely. It was further agreed that the debt of Leyland Bus and Truck would need to be written off this year whatever the outcome of the consideration by the European Commission.

I am copying this letter to Alex Allan (H.M. Treasury).

*Y*  
*Ans,*  
*David*

DAVID NORGROVE

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