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PRIME MINISTER

BRITISH CALEDONIAN

Lord King and Sir Adam Thomson have reached agreement on a "merger" which values British Caledonian at around £240 million. A condition of the deal is that there should be no reference to the MMC. An announcement will be made at 0800 tomorrow and Sir Adam Thomson will be going to see Lord Young at midday.

Sir Adam Thomson argues that British Caledonian's business would be damaged by a reference. There may be something in this, but if it became clear that this was in fact the case, the MMC could terminate its reference or, if it became clear early enough, the OFT could recommend against a reference. There is also, I would think, an element of blackmail.

Either way, it looks as though British Airways cannot lose. Either they win British Caledonian and greatly strengthen their hold on the market, or the deal fails with the market knowing that British Caledonian was looking to be taken over, inevitably damaging its position.

Mr Channon will report the position to Cabinet tomorrow, but I have suggested to his office that he make it absolutely clear that the decision on a reference is one for the Secretary of State for Trade and Industry and for no other member of Cabinet.

DCW  
D R NORGROVE  
15 July 1987

DASAKH

SECRET