

PRIME MINISTER

INMOS

Mr. Tebbit is seeking the views of colleagues on how to proceed with INMOS. He argues that the bid from AT & T is insufficient and suggests an alternative path of seeking institutional investors into INMOS which would dilute the Government's stake.

Policy Unit agree that the AT & T bid is sufficient but rather than proceed to an injection of funds from UK institutions, they think a more active search for buyers should be undertaken first.

* (Dr. Nicholson, however, supports the idea of institutional investment to create an independent UK company.

Do you wish to express a view at this stage? When colleagues have commented we may need a meeting.

AT

I agree - but hope that at least 75% of BT's holdings can be sold off in the operation.

Andrew Turnbull
2 March 1984

INMOS file

Possibility of sale of INMOS to a US firm

Line to take

INMOS needs more money to capitalise on its trading success and develop further products, the company having moved into profit at the end of last quarter. New funds must come from the private sector, the taxpayer having met the start up costs. It is for the BTG, who own 75% of INMOS, to work with the company to raise this additional finance and they are having discussions with several interested parties at present. I very much hope finance will come from this country; INMOS' technology is important and our IT industry needs access to the sort of products it is developing.

I pressed on AT & T. The BTG will consult us on where additional finance is to come from but we have had no proposals from them yet. Discussions are continuing with a number of people. In looking at any proposal, however, who owns the company is not the only consideration; of equal importance is what is being produced where.7

BACKGROUND

Articles appeared in the Sunday Times on 5 February and the Financial Times on 6 February about the possibility of INMOS being sold to an American concern. The Sunday Times article contained several inaccuracies and implied that a decision had effectively been taken. This is not so. A revised offer from AT & T (which was higher than one made in January) was received at the end of last week but present indications are that it does not value the company as highly as other proposals being considered which would not involve control passing overseas. These proposals involve placing minority stakes with combinations of an American company, UK companies and financial institutions. A public offer for sale in the next 18 months has not been ruled out, and contrary to the Sunday Times, GEC have had ample opportunity to make an offer but have declined to do so even though they have received all the information supplied to others interested.

The Secretary of State for Trade and Industry has been briefed on the AT & T offer and will be seeing the company on 9 February. He will make it clear however that he is not there to negotiate on the terms of an offer; AT & T must pursue that with Sir Malcolm Wilcox, Chairman of INMOS and Board Member of BTG.

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Sir Clive Sinclair pointed out at your Lancaster House Seminar that the UK IT industry must have ready access to the latest, most sophisticated components if it is to design and produce world competitive IT products. The key to his low-cost computers has been Ferranti's Uncommitted Logic Array. Inmos components, such as their current memory products and their revolutionary Transputer are the basis of some of tomorrow's new IT products, ranging from inexpensive consumer goods to enormously powerful parallel processing computers.

2. Inmos is now successful despite its unpropitious origins because of the brilliance of its design team at Bristol and the ready access they have to state-of-the-art silicon processing know-how in the Colorado Springs unit and a modern manufacturing unit at Newport. As the Colorado Springs know-how is transferred to the UK units, they will become a unique design-through-to-manufacturing capability in the UK. The quality of the team and the facilities are such that there must be a good expectation that a succession of highly innovative components will flow from Inmos which will not only be a substantial business in their own right but will also offer the UK IT industry an inside track in developing a wide range of new chip-based products. Inmos's capability would be lost if chip design was separated from processing and manufacturing know-how.

3. The Inmos design team are entrepreneurial in spirit and working methods - this is the basis of their success. They

could not remain effective under A.T. & T. and would disperse - no doubt A.T. & T. realise this which is why their offered price discounts the design capability of Inmos and only reflects the value of the Newport manufacturing facility. A further argument against American control is strategic - there is increasing concern about the current tightening-up on American technology exports, coupled with fears, rightly or wrongly, that legitimate security considerations are being used to gain commercial advantage for US companies.

4. It would require rare enlightened management from any large company, even British or European, to maintain the current effectiveness of the Inmos design team and I wouldn't back GEC or Siemens in this regard. Inmos's strength is best maintained and developed by fostering its independence as a company. This points to a round of institutional investment to dilute the BTG shareholding to below 50 per cent followed a little later by a public offering of shares in which the BTG holding is finally sold off.

5. I must stress that Inmos is now a superb and respected technological asset in the UK which, properly maintained and used, can become a significant pace-setter in the UK's IT industry. I believe Mr Tebbit's proposals would have this result.

6. I am copying this minute to Sir Robert Armstrong.

RBN

ROBIN B NICHOLSON
Chief Scientific Adviser

Cabinet Office
2 March 1984



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2 March 1984
Policy Unit

PRIME MINISTER

File

INMOS

Norman Tebbit's paper seeks some advice.

There are two possible routes that can be pursued.

1. Seeking a buyer for INMOS at this stage. AT&T have come forward with a bid which is judged inadequate.

This route, however, has many attractions. It takes further funding risk away from the taxpayer, providing once-and-for-all limitation on the Government's commitment. There could be some guarantees that work would remain in the UK, and AT&T have themselves pledged further monies for development, including investment in South Wales. If AT&T are prepared to make two offers within a reasonable space of time, it is likely that others also will up their offers or come into the bidding if they are encouraged to do so by the Government and BTG. Shouldn't we pursue this line to see if more players come in, and whether a better offer can be achieved?

2. Institutional funding and partial sale of the equity. There are dangers in pursuing this route. INMOS has always been a cash-hungry business, and is likely to remain so. It intends to rely on continually pushing forward the frontiers of technology, which requires major investments in R&D. The shelf life of each product it develops may be quite short, the competitive pressures build up quickly, and marketing has to be good to make money during the period of maximum popularity for the product.

The institutional funding route is uncertain because:

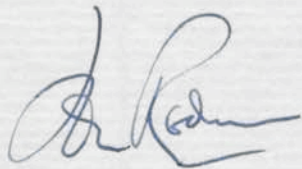
- (a) The terms for raising money early this year may make it more difficult to raise money later on.
- (b) BTG would remain the main shareholder. It would therefore be the prime risk-carrier. The market for chips could fall. The transputer could disappoint. The dividing line between profit and loss is very thin. Development costs for the new range of products could escalate.

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- (c) The institutions might become disheartened if the results were not satisfactory over the next few months, and this would make raising more money difficult.

We recommend:

1. You do not rule out the possibility of complete sale, even if the bidder is an overseas buyer. This could be the best answer.
2. AT&T do not want the transputer. Why couldn't this stay British? Several other UK firms have manufacturing and research capability.
3. Has anyone negotiated professionally with AT&T and other suitors in order to meet concerns about UK technology and employment?
4. Could the DTI tell us more about the other prospective bidders and their offers? We believe another major US corporation has also made an interesting offer.
5. Should not DTI spell out the financial risks of the institutional route more clearly? INOMS on their analysis needs £75 million more, a considerably larger sum than currently under discussion with institutions.



JOHN REDWOOD