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10 DOWNING STREET

From the Private Secretary

10 June 1985

Dear John,

BL/HONDA

The Prime Minister has seen your Secretary of State's minute of 6 June. She agrees with your Secretary of State that leaks like the one in the Financial Times referred to in your Secretary of State's minute are damaging, and particularly so when commercial negotiations are involved. She welcomes the steps your Secretary of State is taking to stop unauthorised disclosures from within BL, the Department and its advisers.

The Prime Minister has asked me to say that she has been assured, and firmly believes, that none of the leaks have come from within No.10, and that none will. The few people involved here handle a wide range of material of this sort which does not leak; and they are deeply conscious of the damage to the Government's standing and policies, and to their own relationship and trust with herself and departments, which responsibility for a leak of this sort would do. The allegation in the article in this week's Spectator, to which you drew my attention on Thursday evening, that Mr. Redwood and Mr. Warry of the Policy Unit here have been leaking such material to the Financial Times has no foundation, and we are consulting the Law Officers and the Secretary of the Cabinet about the terms of a letter which would correct these allegations.

The Prime Minister certainly does not believe that the nature of the views described in the Financial Times' article gives a reliable clue to the source of the information. She has noted that a number of the elements in the story have already been the subject of earlier reports. For example, references were made to Honda's Swindon plans in the Financial Times of 23 April and the possbility that the new small engine could be acquired from Honda was reported in the Financial Times of 4 May and has been discussed publicly by one of the department's advisers (Financial Times of 11 May). In the light of this, without qualifying at all her condemnation of such leaks, the Prime Minister is a little surprised that Honda should have reacted so adversely to the article in last week's Financial Times, particularly when it would appear to provide an opportunity for them to increase their sales. But she hopes that the talks between BL and Honda will now

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progress smoothly and that the necessary consideration of all reasonable options will not be obstructed by further incidents of this sort.

I am copying this letter to Rachel Lomax (HM Treasury) and Leigh Lewis (Minister without Portfolio).

Yours sincerely

Andrew Turnbull

Andrew Turnbull

John Mogg, Esq.,
Department of Trade and Industry

10 DOWNING STREET

From the Private Secretary

Prime Minister

Mr Tebbit is angry about yesterday's FT story on BL and blames it for causing difficulties (somewhat illogically) in the discussions with Honda. He is clearly pointing the finger at the Policy Unit.

Possibly coincidentally, possibly not, the Spectator is running an article on the Policy Unit which makes the accusation of leaks by it on BL explicit.

Whatever the rights and wrongs of this case (and motive does not point to the Policy Unit), you may want to discuss with John its contacts with the Press, and emphasise the need for the Unit to be extremely circumspect. Even if untrue, accusations by your colleagues that they are being leaked against can only be harmful.

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PRIME MINISTER

BL/HONDA

Austin Rover delivered the letter, whose text you approved, to Honda in Tokyo yesterday, 5 June, and had a discussion with Mr Kume, the Chairman of the company. It appears that the company were acutely embarrassed and compromised by the story in yesterday's Financial Times which they assumed to represent the views of the Government. The reports were taken by some members of the Honda Board to indicate that Mr Kume and his immediate colleagues had committed Honda, in the draft Memorandum of Understanding with BL about collaboration, to build an engine plant at Swindon on which the Board had not yet decided. The leaks therefore hit a particularly raw nerve within Honda. There was acute confusion about the intentions of the British Government, which they assumed the Financial Times article to represent; and they emphasised the basis of the long term understanding they had with Austin Rover, which was that the two companies should maintain their separate identities and that Honda were not willing on any basis to share their engine technology. The first session of the talks was exceedingly uncomfortable and came close, in ARG's view, to termination of all collaboration between the two companies.

After a long recess, Honda confirmed they were willing to continue discussions about collaboration and remained surprised and puzzled about why the request on engines had been made. They stressed that they were not willing to collaborate on engines or to allow manufacture under licence, but needed more time to consider how the request to supply an engine might affect their intended collaboration with BL. A reply to the ARG letter will be coming back to the UK over the weekend, but this may not contain an answer. A senior member of the Honda management will be coming to the UK towards the end of next week and this may clarify the position.

Meanwhile, it is clear that the story in the Financial Times has been most damaging to the relationship between ARG and Honda, and endangered the whole basis of future collaboration between them. I am disturbed and angry that this should have happened. I do not, of course, know where the Financial Times obtained their material, but it is clear that the views expressed towards the end of it do not represent the views of ARG, of my Department or of myself.

Any further leak which appears to represent the views of the British Government within the next week or so could well be the last straw for Honda. I am giving instructions in my own

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Department that there should be a complete blackout on information and opinions about the BL/Honda collaboration until decisions are reached and publicly announced, and I should be most grateful if my colleagues could do likewise. I am taking steps to ensure that BL observe a similar total embargo.

I am sending copies of this minute to Nigel Lawson and Lord Young.

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6 June 1985

Department of Trade & Industry

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change "too cheaply." To loud applause Sir Nicholas said he would convey their view to Mr Robin Leigh-Pemberton, Governor of the Bank of England, without delay.

The exchange and the Bank have been trying to keep the cost of entry of outsiders to no more than £700,000 so as not to deter potential participants from using the exchange.

A surprise intervention came at yesterday's meeting from Mr Jeremy Lewis, a partner with stockbroker Seymour Pierce and a member of the ruling council. Mr Lewis was on the five-man constitutional committee which had drafted the proposals for Resolution 2. He urged members to vote against the resolution as the constitutional issues needed to be explored in greater detail.

One broker urged that the meeting and the vote should be adjourned until September but that was rejected by Sir Nicholas.

He asked the members present to vote on the resolutions by a show of hands, which one broker estimated went 80 to 90 per cent in favour of resolution 1 and about 70 per cent in favour of resolution 2. A full vote of the entire membership will be taken in a poll today and no count was taken.

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target range of 5 to 9 per cent. The annual growth rate over the last three months was 19 per cent.

Figures due out later this month are widely expected to show a further acceleration in the annual inflation rate, perhaps to 7¼ per cent. That would leave room for only a very small—perhaps ¼ point—cut in base rates.

Broker James Capel estimated that if the Treasury was to meet its target of keeping sterling M3's average annual growth rate over 1985-86 down to 9 per cent or below, there was scope for monthly increases of only ¾ per cent for the rest of the year.

In Whitehall, however, officials were playing down the significance of the recent strong growth in the broad money supply measure and of

Cost of Pilkington job cuts to rise

BY IAN RODGER

THE COST of financing redundancies at Pilkington Brothers, the leading UK glass-making group, will rise to £31m in the next two years. The group has already spent more than £60m on reducing its workforce over the past five years.

It had been widely assumed that Pilkington's redundancy charges were on a downward trend, especially since the £104.8m rights issue last December.

However, Mr Antony Pilkington, the chairman, said yesterday that the group had identified all the positions it needed to eliminate so as to make its glass and fibre-glass plants among the most productive in the world. "So we have decided to have one last big push to persuade people to go. Then we will be finished."

The group next week publishes its preliminary financial results for the year to March 31, 1985, in which it will indicate that redundancy charges will amount to about £20m this year and another £11m in 1986. Pilkington has halved the 18,000 workforce at its main manufacturing base in St Helens, Merseyside, over the past five years, but another 2,000 jobs are to go.

Mr Pilkington said redundancy charges were a form of capital investment for the group. Money spent on this in the past few years had helped bring about substantial increases in profits through improved productivity. UK trading profits more than doubled to £11.6m in the first half of the current year against a background of falling prices and weak demand for many Pilkington products. He predicted that the pay-off from the new redundancy programme would start in 1986.

Mr Pilkington acknowledged that the group could be criticised for having taken a long time, by comparison with other leading UK manufacturing companies, to reduce its manning to international levels.

However, he said the group had been constrained by the concentration of most of its factories in the St Helen's area. "We have an important civic responsibility. We can't just pass on our problems to the local authorities."

"The difficult thing is to shake up working practices and manning levels while keeping a happy company," he said.

BL plan agreed subject to Honda engine deal

FINANCIAL TIMES REPORTER

THE GOVERNMENT is understood to have approved BL'sfive-year corporate plan, subject to BL's agreement that Austin Rover, its volume cars company, purchase from Honda of Japan engines and gearboxes needed for its end-of-decade Metro replacement.

Such a move could cut about £250m from BLs planned £1.8bn investment programme. It would run counter to the known wish of Mr Harold Musgrove, Austin Rover's chairman, that his company retain the ability to design its own engines.

Given that the key request about the Honda engine is met, the Government is thought to be ready to:

● Support a proposal that Austin Rover assemble Honda cars under contract. The first cars would go into the Longbridge plant at Birmingham next year.

● Agree that a middle-range car, code-named the YY, be developed jointly by Austin Rover and Honda. The YY would eventually replace Maestro and Rover 200 models.

The recommendation that BL seek an engines deal with Honda was made by the Department of Trade and Industry, which has been studying the BL corporate plan since it was submitted in November.

It reflects the Department's concern about Austin Rover's market performance, and was one of a series of possible economies originally suggested by the policy unit of 10 Downing Street.

The idea was first rejected by BL. Mr Musgrove is expected to open talks with Honda, but the possibility of a deal eventually being struck remains in doubt.

The Austin Rover chairman has said that without the ability to design its own engines, the UK would become a mere assembler, dependent on outside technology.

This has become a political issue, with the Labour Party and the trade unions backing Mr Musgrove's belief that engine design and construction capability should be retained by Austin Rover.

Support seems to have grown within the Government for the view that increased Honda and Austin Rover collaboration would strengthen the state-owned company in the short term; and pave the way for eventual privatisation.

It is stated that there would be no overall loss of jobs at Longbridge, where the Metro engines and gearboxes are manufactured because additional labour would be required to assemble Honda cars.

A Metro replacement with an Austin Rover body design and a Japanese engine (Honda enjoys a high reputation for quality) is thought likely to prove a success in the market place. This is seen as the key to Austin Rover's future viability, and to job security in the dependent components industry.

Honda engines would be manufactured at Swindon, Wiltshire, where the Japanese company has acquired a site. Materials would be supplied in the UK rather than imported.

Where the assembly of Honda cars under contract is concerned, Austin Rover would have to invest more than £30m in facilities. The proposal states that volume could climb to about 100,000 a year within three years. Honda would have no equity stake.

For Austin Rover the deal would provide better throughput for its existing production facilities, which are underused. For Honda, a platform would be provided from which it could sell into the European Economic Community.

Despite the resolution of most of the corporate plan difficulties between the Government and Austin Rover, the precise position of Honda in relation to the plan does not appear to have been finalised, except for agreement on joint development of the mid-range YY car to succeed the Maestro.

Honda sells 100,000 cars a year in Europe. It is open to question whether its dealer infrastructure could readily handle doubling of supplies.

Further, it is questioned whether the market could absorb 100,000 a year of one particular model, even with variants, which would provide the most advantageous economies of scale.

The viability, on production cost grounds, of dividing output between two models could also be questioned.

Nor is it clear whether Honda really would be prepared to rely on Austin Rover for such a large potential proportion of its sales. It is, for example, investing substantially in its 330-acre site at Swindon for post-production testing and checking of the joint XX executive cars.

The proposal could be seen as not necessarily meshing in well with its long-term plans to set up its own vehicle production plant on the Swindon site.

It is understood that Honda is more than willing to enter an agreement with Austin Rover to supply engines for the Metro replacement from Swindon.

This would strengthen its plans for engine manufacture at the site, which could include production of the engine now imported from Japan.

6 June 1985

MR TURNBULL

THE BL/HONDA PRESS REPORTS

As you will be aware, there have been a long line of detailed but misleading press reports about the BL Corporate Plan over the last 3 months. With the exception of a report in yesterday's Financial Times, almost all of these have been unhelpful or, at best, neutral for the policy line that the Unit was taking. BL unions and Labour MPs have appeared well-briefed on the subject, and I understand that many of the reports first occurred in the Birmingham press. You will recall that Dan Jones - the economist employed by Barings to review the BL Plan - was also reported as making some very explicit comments on the Plan.

The innuendo in Norman Tebbit's letter is that No.10 has been responsible for this latest leak. The Spectator is carrying an article suggesting that John Redwood and I have been responsible for leaks over the past 2 months. Neither John Redwood nor I have given any stories to the press on BL, nor have we been the source of these stories. It is noteworthy that the Spectator article - which DTI knew about in advance - was written before the FT story yesterday, which is the only one that has ever come near to being helpful to the Policy Unit line.

Why Honda should be "embarrassed", still less threatening to call off collaboration when they are being offered more business is difficult to understand. AT

It is difficult to understand the "embarrassment" that Norman Tebbit claims the FT article has caused Honda. Honda's intentions on collaboration with BL have been well publicised: they even held a press conference when they broke the first ground at the Swindon plant. And as the article came far closer than any previous press coverage to accurately reporting what is meant to be the Government's position on negotiations with Honda, it is surprising that it could have caused "acute confusion about the intentions of the British Government".

Peter Warry

PETER WARRY