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Secretary of State for Industry

*copies to: Mr Wolfson
Mr Walker
Ms Hodgson*

*I suggest we be
fairly tough. other companies*

16 April 1981

The Rt Hon Sir Geoffrey Howe QC MP
Chancellor of the Exchequer
HM Treasury
Parliament Street,
London SW1P 3HE

*have to operate in
unfavourable conditions
my*

Prime Minister.

*Agree with Sir Keith Joseph
should proceed as he proposes or
X / below? I understand that the
Chancellor is likely to go along
with the suggestion reply to the
BL Board - RHW 24w.*

John Geoffrey.

BL'S FINANCIAL POSITION

I attach a letter dated 10 April which the Chairman of BL has sent me about BL's prospects.

2 You will see that the BL Board believe that economic conditions - in terms of both currency levels and economic activity - are significantly worse than assumed in the Corporate Plan. Internal performance, on the other hand, is satisfactory and indeed better than predicted in several key respects; for example, manpower at end February was 4000 lower than the budget figure and UK market share is running well above forecast (20.7% for cars up to the end of March compared with the budget of 18.5% for the same period - and this is on a rising trend with 23.1% in the whole of March).

3 The Chairman's letter is based on the first monitoring report for 1981, covering both January and February. Treasury officials have copies of this material and were present at the regular meeting with BL at staff level. I understand that the BL Board did not accept the revised forecasts for the whole of 1981 prepared by their staff, partly because the economic assumptions made were still somewhat optimistic, but partly because they had assumed that no corrective action would be taken. In fact the Board plan early and harsh corrective action (of which I have some preliminary details but expect to hear more on 12 May) involving significant accelerated closures, sharper manpower reductions and increased pressure on suppliers.

4 For these and other reasons set out in the letter, the BL Board have concluded that it would be premature to initiate a formal review of the Corporate Plan within the terms of the Chairman's letter of 26 January.

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5 We need to decide now how to react to the Board's decision. The purpose of a formal review, if one were instituted, would be to decide on corrective action if that were possible, or on closure if not. It is clear that the Board already have corrective action in hand. As for closure, whatever our individual attitudes at the time, our collective decision in January on the balance of arguments was to keep BL alive. The question now is whether the balance of arguments has changed decisively. BL's internal performance and market share are rather better than the company's management or we expected. The external prospect in their view is somewhat worse: but I think it would be difficult for us to argue that the longer term economic prospects have changed so significantly since January as to destroy what prospect there is of recovery, especially since vigorous and early corrective action is planned. I therefore propose, if you and the Prime Minister agree, to tell the Chairman that I accept the Board's decision for the present. But I propose to say also that we shall be reconsidering the position in the light of the specific corrective action notified to us in mid-May and that we shall continue to monitor closely BL's monthly results and revised forecasts for the year in the light of economic prospects at the time.

6 I am sending copies of this letter to the Prime Minister, Jim Prior, Sir Robert Armstrong and Robin Ibbs.

Ever,

Kear

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01-486 6000

13 APR 1981
SECRETARY OF STATE
FOR INDUSTRY'S OFFICE

35-38 PORTMAN SQUARE

LONDON W1H 0HQ

10 April 81.

FROM SIR MICHAEL EDWARDES

The Rt.Hon. Sir Keith Joseph, Bt,MP,
Secretary of State for Industry,
Ashdown House,
123 Victoria Street,
London SW1.

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New Secretary of State,

IMPACT OF ECONOMIC OUTLOOK ON BL

Further to my letter of 11th March, the Board has now had an opportunity to consider the status of our 1981 Corporate Plan in the light of the present economic outlook, including the impact of the March Budget.

Volume

The Board believe that the immediate economic outlook has deteriorated substantially since the 1981 Plan was submitted to the Government. We now forecast that the UK car market will fall to 1.375m in 1981, compared with 1.42m in our Plan, and the decline in the UK truck market is even more severe. In addition, the developing trend towards smaller cars is likely to be accentuated by the Budget; this change in sales mix helps Metro, of course, but damages overall profitability because of the lower margins obtainable in this sector of the market. I should add that both our Plan and our latest forecasts have been broadly in line with motor industry forecasts.

Continued

The Rt.Hon. Sir Keith Joseph, Bt,MP,
Secretary of State for Industry.

2.

Sterling

The other economic factor which is showing a substantial deviation from the assumptions in our Plan is the level of sterling. Not only has the trade-weighted rate so far remained substantially higher than our forecast; but even more important to BL is the particular strength of sterling against the European currencies, at a time when we are launching our new car and truck models into Europe.

Revised Assumptions

The Board concluded that the Government should be informed of the deterioration in these aspects of the external environment assumed in our Plan for 1981. We also considered whether it would be appropriate to agree at this stage on a new set of more pessimistic assumptions for the later years of the Plan and to review the strategies for the four main business groups accordingly, as provided in my letter to you of 26th January. The Board decided that such action would be premature, for three main reasons:-

1. The uncertainties about the economic outlook after 1981 are so great that we believe we are not in a position at this stage to take a firm view, even though many of the assumptions in our 1981 Plan now look optimistic compared with most recent external forecasts. However, BL staff are opening discussions with your officials on the economic assumptions which we shall have to establish in due course for the compilation of our 1982 Plan.
2. BL's trading performance in the first two months of 1981 was broadly in line with the Plan. Nonetheless, we are already in the process of developing action programmes, with the objectives both of offsetting the additional cash outflow caused by the deterioration in the economic situation, and of improving our competitiveness in future years. These actions

Continued

/These actions

are likely to include further reductions in manpower, additional or accelerated plant closures and further pressure on the prices of our component suppliers (with re-sourcing overseas where necessary). Our current financial projections for 1981 as a whole take no account of the impact of these measures. Some of these actions will be painful and controversial, and a meeting between us has been provisionally arranged for 12th May so that I can give you advance warning of any "sensitive" actions we may need to announce at or before the Annual General Meeting on 14th May. These actions are unlikely to represent any fundamental change to our strategy, apart from timing.

3. In the Leyland Group, where there has been a particularly substantial shortfall from the forecasts incorporated in our 1981 Corporate Plan, the Plan is in any event already under review. You will recall that the original Plan for the Leyland Group was intended only as an indicative document, to be reviewed by the new management team which is now fully in the saddle. The revised Leyland Group Plan (which will be submitted to the BL Board in May and thereafter forwarded to the Government) will, of course, include actions designed to improve the profit and cash outlook for the Leyland Group, in so far as the severe recession in the commercial vehicle market allows. For action purposes, this Plan will have to be based on updated and therefore tougher economic assumptions covering the full Plan period 1981-85. While these are acceptable for immediate operational decision-making, we would not want to rely on them when making long-term judgements about the Leyland Group, as there is no certain foundation for the economic assumptions.

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The Rt.Hon. Sir Keith Joseph, Bt,MP,
Secretary of State for Industry.

4.

To summarise: The external economic environment makes life more difficult for us, but, until we are clearer as to the impact of the Government's policies and actions on medium term economic prospects, we will not be proposing a major review of the Plan other than that already in hand for the Leyland Group. In the meantime, we are stepping up our streamlining programme.

I trust that the Board's overall approach and our tentative arrangements to meet on 12th May are acceptable to you.

Yours sincerely,
Michael Power.