

PRIME MINISTER

MIDLAND BANK

The Midland Bank wish to announce first thing on Tuesday a restructuring package designed to put them on the road back to prosperity. The package would comprise:

- a rights issue;
- substantially higher provision for Third World debt;
- sale of the Clydesdale Bank to National Australia Bank.

The assessment is that this would be good news for the Midland and greatly improve their status from a prudential point of view.

The obvious political problem is the effect in Scotland. It would be possible to argue that Clydesdale run by an Australian bank would be more independent in practice than Clydesdale under the close eye of the Midland. This would help, but Scottish MPs and others are bound to seize the opportunity to make trouble.

There is great time pressure, of course. Aside from the timing of the formal announcement, Kit McMahon plans to see the Clydesdale management tomorrow morning (they know nothing of this as yet) and then to see Malcolm Rifkind to try to put the advantages of the deal to him.

The Government has a role in two possible ways.

First, the Banking Act includes reciprocity powers. These do not come into force until 1 October, but they could, with some awkwardness, possibly be made to act retrospectively. This, however, looks a most unattractive option.

Secondly, there is the MMC. The Chancellor believes it will be difficult not to refer the bid to the MMC on public

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interest grounds. In part, this is because Lord Young said, during the passage of the Banking Bill in April, that:

"It is almost impossible to conceive that an overseas bid for a United Kingdom bank would not be referred."

He was no doubt then thinking of the major Clearing Banks, but Clydesdale is also a Clearing Bank. His statement will have all the more weight because of his present position.

I am told that the Chancellor may be inclined to suggest a meeting, which you would chair, with himself, Lord Young and Mr Rifkind. I am dubious about this: Mr Rifkind is bound to take an intransigent position and, against your normal practice, you would be drawn into the centre of the decision on a referral. I suggest it would be better for your opinions to be made known to Lord Young through the Chancellor rather than directly.

There are still some questions of fact which you will want to explore, including the role of the Director General of Fair Trading, and whether Lord Young can take a decision against his advice under the circumstances of a case like this, based on public interest. But a referral does look difficult to avoid.

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1 July 1987

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