

PREM 19/163

42.37

PART 3

SECRET

Confidential filing.

The Defence Budget. Statement on the
Defence Estimates 1980.

DEFENCE.

United Kingdom MILITARY Training
Assistance SCHEME (UKMTAS) [Table of UK Arms
subs.]

Pt 1 May 1979

Defence Statics in folders
attached

Pt 3 January 1980.

Referred to	Date	Referred to	Date	Referred to	Date	Referred to	Date
23.1.80.		8.10.80					
3.1.80		16.10.80					
31.1.80		<u>ends</u>					
5.2.80							
11.2.80							
20.2.80							
21.2.80							
3.3.80							
4.3.80							
23.4.80							
24.4.80.							
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8.8.80							
10.9.80							
2.10.80							
8.10.80							
28.10.80							

PREM 19/163

Defence Statistics in folders attached

● PART 3 ends:-

MISC 42(80) 28. 16.10.80.

~~CST to S/S Defence 8.10.80~~

PART 4 begins:-

HMT to TPL 17.10.80

~~S/S Defence to PM 23.10.80~~



Defence

Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon Francis Pym MC MP
 Secretary of State
 Ministry of Defence
 Main Building
 Whitehall
 London SW1A 2HB

8 October 1980

Dear Secretary of State,

THE DEFENCE PROGRAMME

I have seen a copy of your minute of 3 October to the Prime Minister and members of OD about your cash limits in the current year.

As you know from our talk on 29 September, I am concerned at the evidence that, despite the measures you have taken, your expenditure is still running well above the level consistent with the increased cash limit total which was agreed and announced in early August. I have since seen end-September cash figures, which confirm that there is still no sign of a down-turn in your rate of spend, and suggest that you are still on course for an overspend of at least £250 million.

You told me on 29 September that it is your firm objective to stay within the cash limit. I have to say - in the context of the penultimate paragraph of your minute - that it seems clear to me that this will undoubtedly entail your taking further measures to restrain expenditure. A third consecutive breach of the Defence cash limit would be very damaging. And the sooner sufficient further measures are implemented, the better; for the later in the financial year you introduce them, the more substantial they will have to be. It also seems to me that something more than adjustments in the arrangements for making payments to your suppliers will be needed; but of course it is for you to say.

The situation has deteriorated since our discussion and probably since your minute of 3 October was drafted. I hope that you will be able to confirm that sufficient further measures are being introduced. It would be helpful if you could list them when you send to the Treasury the revised expenditure profiles mentioned in your Private Secretary's letter of 2 October to No 10.

Copies of this letter go to all the recipients of your minute.

Yours sincerely
T. Matthews (Private Secretary)
 P.P. JOHN BIFFEN

[Approved by the Chief Secretary and signed in his absence]

-8 OCT 1980



MO 8/2/12

PRIME MINISTER
THE DEFENCE PROGRAMME

A report from Mr Pym on the effects of this year's defence cut-backs. See also the Chief Secretary's comments at Flag A - he thinks further measures will be needed if Mod are to stay within their cash limit. We understand that Lt. Carrington is very concerned about our position vis-a-vis our allies if further volume cuts are made.

Following our discussions in August I believe that I should report the measures I have taken to restrain expenditure in the current financial year within the increased defence cash limit.

I started from a position where I had already authorised two tranches of reductions to save about £250M and so remove the unplanned growth in this year's programme caused by the industrial recession - the deferment of equipment projects, a major cut-back in the works programme, reduction in stocks, fuel savings and the postponement of schemes such as Assisted House Purchase. After allowing for the uplift in the cash limit agreed last month I was left with a substantial gap to be closed.

As an immediate step I imposed, initially for three months, a moratorium on all but essential defence contracts. To produce the necessary savings this had to be comprehensive applying to extra-mural research and development, capital equipment, lands, buildings and new construction, and the purchases of spares, stocks and reserves and repairs. I had, of course, to exempt the strategic nuclear deterrent and those contracts whose cancellation or deferment would have caused disproportionate financial or other penalty.

This should save £100M this year. The non financial cost is that the Services will within a few months begin to feel the effect of shortages of spares, and the reduced level of maintenance and repair; if long term damage is to be avoided the position must be recovered as early as possible next year.

There has also been political damage, particularly at the local level. I have been at pains to explain to industry, to trades and employers' associations why the moratorium has been necessary. I have found a measure of sympathy - senior industrial management at least are well aware of the difficulties of managing cash flow in a large organisation - but almost without exception this reduction in the flow of funds to industry is seen as a further shift from the public sector to the private



of the burden of the recession. Firms see high interest rates - for which they hold the Government directly responsible - and the economic recession as combining to create cash flow problems for them of a kind which force them to accelerate work on defence contracts. Redundancies in the defence sector are inevitable and some firms particularly subcontractors may go under. The apparent illogicality of forcing firms to borrow more money from the banks or to lay off workers, and put up the cost of unemployment benefit, in order to reduce defence expenditure is not lost on them, and will need the most careful handling when Parliament reassembles.

To find a further £100M this year I have also authorised cuts in personnel movements and freight, made savings in the purchase of nuclear materials, and made a major cut in planned fuel purchase. This will mean a substantial reduction in activity by all the armed Services during the remainder of the year. The time the Fleet spends at sea, and flying by the Air Transport Force and by the Long Range Maritime Patrol Force will be cut by 30%. Hydrographic surveys and offshore oil and gas rig patrols will be cut by 25%; collective Army training in the UK and Germany by between 35 and 45%; TA training by 25% and certain other forms of Army training by up to 30%. Our participation in NATO exercises will have to be reduced.

The measures outlined above inevitably involve a significant short term deterioration in the operational readiness and capability of our forces. In the very short term this is a risk which we have to run and we must pray that the situation in Northern Ireland remains calm and that we do not have to deploy forces elsewhere over the next few months. But they run absolutely and directly counter to the military need.

I have also had to authorise a drawing down of our war reserves of fuel (by $\frac{1}{4}$ in the case of the Army and the RAF) below the levels called for by NATO. Events in the Middle East underline the significance of this action, but I do not believe that less damaging savings that would have an effect this year can be found elsewhere. I shall however be monitoring the position very carefully.



I am continuing to keep expenditure under very careful review. Later this month I shall decide on the future of the contracts moratorium after the initial three month period expires on 8th November, and also whether further measures can and should be taken to restrain expenditure. My present view is that the moratorium in its existing form, although the only weapon available to me that would secure savings early enough in the financial year, would cause unacceptable damage to industry if continued too long and will have to be replaced by a somewhat different (but nevertheless very stringent) regime.

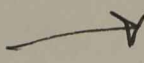
We are discussing with industry now the implications for defence suppliers of our very tight cash position, and we are trying to devise further ways of slowing down our cash flow for the rest of this year. To the extent that we are postponing necessary expenditure - whether by the moratorium or other means - this will increase the financial pressure next year. I am having to give very serious thought to how much money will be needed next year to support the programme we agreed in OD and to restore the temporary damage done this year. I am discussing this with the Chief Secretary.

I am sending copies of this minute to other members of OD, to the Secretaries of State for Industry and Employment and to Sir Robert Armstrong.

3rd October 1980

Ministry of Defence

T.P.M:d
Def. Exp
A.S



Copy - to see

Reference



del
bx.

MINISTRY OF DEFENCE
MAIN BUILDING WHITEHALL LONDON SW1
Telephone 01-9307622 218 2111/3

MO 8/2/12

2nd October 1980

Prime Minister

mb.

These figures seem to show that MoD will need to make further cuts if they are to stay within their revised cash limit.

Dear Tim,

In reply to your letter of 10th September I enclose a Table 1 a summary of figures reported so far this financial year through the Financial Information System for each of the five Defence Votes. You will see that we are now able to provide such figures to the end of August. They are annotated to show the equivalent percentages of the original cash limit or Estimates provision. For total expenditure, percentage figures are also given of the revised defence cash limit and revised total defence provision.

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2/10
(Mr Pym will be sending a further report in the next few days)

In addition, I enclose as Table 2 a summary of the monthly percentages of final outturn which, on previous experience, we would have expected to provide a broad basis for monitoring the reported figures. I should make clear however that the percentage profile in this table is now unrepresentative of probable cashflow during the remainder of this financial year. Further cuts are necessary to bring expenditure in 1980/81 within the revised defence cash limit. These are being achieved both by specific reductions in the defence programme and by means of the moratorium on new defence contracts. We are calculating the effect of this action on future monthly cash flow and shall be producing new percentage profiles as soon as possible which will reflect our best immediate assessment of the likely distribution of remaining expenditure by Vote and by period, adjusted to take account of the revised cash limits. Our object is to bring total expenditure back as soon as possible to a path corresponding to that in Table 2.

I am sending a copy of this letter to Terry Mathews (Chief Secretary's office).

Yours ever,
(Signature)

(D B OMAND)

T P Lankester Esq

FIGURES REPORTED UNDER THE FINANCIAL INFORMATION SYSTEM (FIS)

TABLE 1

	END OF	APRIL	MAY	JUNE	JULY	AUGUST
VOTE 1: <u>Military, Civilian Pay etc</u> Reported cumulative FIS (bookings plus suspense) Percentage of original cash limit		383.1 8.3%	768.9 16.6%	1124.7 24.3%	1516.8 33.4%	1957.2 42.3%
	VOTE 2: <u>Defence Procurement</u> Reported cumulative FIS (bookings plus suspense) Percentage of original cash limit	472.1 10.6%	878.0 19.7%	1281.7 28.7%	1753.4 39.3%	2143.7 48.0%
VOTE 4: <u>Defence Accommodation Services</u> Reported cumulative FIS (bookings plus suspense) Percentage of original cash limit		34.5 5.4%	85.9 13.3%	137.2 21.3%	184.0 28.6%	256.2 33.8%
	VOTE 5: <u>Dockyard Services</u> Reported cumulative FIS (bookings plus suspense) Percentage of original cash limit	23.6 6.0%	50.3 12.7%	75.7 19.2%	112.2 28.4%	144.3 36.5%
TOTAL DEFENCE CASH LIMIT Reported cumulative FIS (bookings plus suspense) Percentage of original cash limit Percentage of revised cash limit		913.3 9.0%	1783.1 17.6%	2619.3 25.9%	3596.4 35.5%	4501.4 44.6%
	VOTE 3: <u>Service Retired Pay, Pensions etc</u> Reported cumulative FIS (bookings plus suspense) Percentage of original cash limit	52.6 9.7%	94.8 17.5%	135.3 24.9%	182.0 33.5%	226.8 41.8%
	TOTAL DEFENCE VOTES Reported cumulative FIS (bookings plus suspense) Percentage of original provision Percentage of revised provision	965.9 9.1%	1877.9 17.6%	2754.6 25.8%	3778.4 34.2%	4728.2 42.8%

REPRESENTATIVE ANNUAL PROFILE: FIS FIGURES

TABLE 2

PERCENTAGE FINAL OUTFURN - End of	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC	JAN	FEB	MAR
Monitoring Profiles												
VOTE 1	9	16	23	33	41	49	58	66	74	83	92	100
VOTE 2	5	12	19	26	34	42	50	57	67	75	84	100
VOTE 4	7	15	22	31	39	47	56	64	73	81	91	100
VOTE 5	5	11	16	24	33	40	48	59	67	74	87	100
Total Defence Cash Limit	7	14	21	29	37	45	54	62	71	79	88	100
VOTE 3	11	18	26	34	42	50	59	66	74	83	90	100
Total Defence Votes	7	14	21	29	38	46	54	62	71	79	88	100

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7 6 5
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-3 OCT 1980



Defence

MINISTRY OF DEFENCE
MAIN BUILDING WHITEHALL LONDON SW1
Telephone 01-~~9307000~~ 218 2111/3

MO 8/2/12

2nd October 1980

Dear Tim,

*R
2/10*

I have written to you separately earlier today about the monthly profiles of defence spending this year. Can I forestall an obvious enquiry by saying that my Secretary of State intends to circulate a report within the next few days setting out the steps which he has taken to restrain defence spending this year, and their implications.

I am copying this letter to Terry Mathews (Chief Secretary's office).

Yours ever,

(D B OMAND)

T P Lankester Esq

MINISTRY OF DEFENCE
MAIN BUILDING, WHITEHALL, LONDON SW1



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- 3 OCT 1980

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Defence

10 September 1980

Against the background of the latest banking figures and the very high central Government borrowing requirement now published for the first five months of the financial year, the Prime Minister has asked if she could see the monthly profile of defence spending so far and planned for the remaining months of 1980/81.

I am sending a copy of this letter to Alistair Pirie (Chief Secretary's Office).

TPLANKESTER

Brian Norbury, Esq.,
Ministry of Defence.

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MR LANCASTER



WITH
THE COMPLIMENTS OF THE
PRIVATE SECRETARY

MINISTRY OF DEFENCE, WHITEHALL

LONDON, S.W.1A 2HB



R

Defence

Mr Hammond

FRIDAY 8th AUGUST 1980

R

MR CRANLEY ONSLOW (CONSERVATIVE) (WOKING)

Mr Onslow

-

To ask the Secretary of State for Defence, whether he will make a further statement on the defence budget.

A N S W E R

(Mr Francis Pym)

My Rt Hon Friend the Chief Secretary has announced that, subject to Parliamentary approval, the Defence cash limit for 1980/81 will be raised by £203M to £10492M. The total defence budget figure will be £11,151M.

This budget allows the Government's defence policy to be developed on the lines set out in Command 7826. But expenditure has been greater so far this financial year than is usual in its first few months because firms have been making faster progress with defence orders and submitting their bills more promptly and prices of equipment have moved ahead faster than expected; I



have, therefore, taken steps to rein in spending. I am also instituting, initially for a period of three months, a moratorium on new defence contracts (save for a few essential exceptions) and I am considering what further measures will be needed to contain spending within the revised cash limit.

Ministry of Defence

8th August 1980

SECRET



SUBJECT.

10 DOWNING STREET

File RP 14.
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Mr Taylor

From the Principal Private Secretary

6 August 1980

Dear Brian,

DEFENCE EXPENDITURE 1980/81

Your Secretary of State called upon the Prime Minister this morning to follow up the meeting which he had had earlier in the day with the Chancellor of the Exchequer to discuss the Defence cash limit for 1980/81.

Mr. Pym said that the Chancellor of the Exchequer had offered an increase in the cash limit of £150m net. He had said in response that he would like to have a further word with the Prime Minister so that he was sure that she was aware of the implications of settling upon an increase of no more than this size. He understood the seriousness of the general economic situation and he was anxious that Defence should make a contribution to the economic recovery of the country. It was in the same spirit that the Chiefs of Staff were approaching the cash limit problem: they were being as helpful as they could, even though some very unpalatable measures such as reductions in ship and aircraft movements would have to be taken in order to bring the programme into line with the new cash limit. The morale of the services was bound to be affected. The primary concern of both himself and the Chiefs of Staff, however, was with 1981/82 and the later years. He had asked the Chancellor at their meeting when we might be able to get back to the NATO commitment of real growth of 3% a year in defence expenditure. The Chancellor had been unable to give any undertaking on this point and had re-emphasised how difficult 1981/82 was likely to be for public expenditure. He understood why the Chancellor was unable to offer any commitment at this stage but he nonetheless wanted to underline the importance of the United Kingdom continuing to give a lead in NATO and therefore of the need to get back to real growth of 3% a year as soon as possible.

The Defence Secretary went on to say that he and the Chancellor had agreed that public presentation of the decision to increase the cash limit by £150m should be as low key as possible. The Chancellor would announce the increase by a Written Answer on Friday, and he would himself let it be known in parallel that he was placing a moratorium on Defence contracts. It would take another 3 weeks or so to identify the other measures that would be needed to rein back the Defence programme and he proposed to let these become public knowledge in as gradual and low key way as possible. It would be important, however, to

/warn other members

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- 2 -

warn other members of the Cabinet of Friday's announcement and to prepare the Party, so far as was possible at the end of the last week before the recess, for what was to come. He proposed to circulate a brief note for tomorrow's meeting of the Cabinet to let colleagues know what decisions had been taken and what their implications were. He hoped that there would be no need for substantive discussion on the note. As regards the Parliamentary Party, he intended to see the officers of the Defence Committee to let them know that, for wider economic reasons, it was necessary to make cuts in the Defence programme. This would come as a surprise to them and they were bound to be disappointed.

As far as NATO was concerned, our position would be devalued once our allies came to understand the consequences of today's decision on the cash limit. Hitherto the Government had played its hand in such a way as to strengthen the alliance to a degree which was greater than our actual military contribution itself. But our ability to continue to do that would almost certainly now be reduced, and we would be thought to be weak when we had appeared to be strong. In reply to the inevitable questions about what our decisions meant for the NATO 3% commitment, he proposed to say that we had been forced to make these changes in our Defence programme by the need to respond to our general economic situation but that we would get back to real growth of 3% a year in our Defence expenditure as soon as we could.

The Prime Minister said that nobody was more disappointed than she that the Defence programme had to be cut and she would not be contemplating this course unless it was absolutely unavoidable. It was, however, vital to keep public expenditure under control if the Government's economic policy was to be successful. If we got the underlying base of the economy right, it would then be much easier to have real growth in Defence expenditure. She accepted a commitment to get back as soon as we could to real growth of 3% a year in Defence spending but she could not say when this would be. She was grateful to the Defence Secretary for acknowledging the need for his programme to make a contribution in the present economic situation and for agreeing that the Defence cash limit for the present year should be increased by no more than £150m. She was also grateful to the Chiefs of Staff for their cooperative approach. She agreed that the Defence Secretary should circulate to his Cabinet colleagues later that day a brief note reporting the decision on the cash limit and describing the implications for the Defence programme. It would be important that nothing leaked before Friday, and Mr. Pym should make it clear that his minute should have only a very restricted circulation. Similarly, he should impress upon the officers of the backbench Defence Committee when he saw them the need for secrecy until the announcement was made. The public presentation of the decision on the cash limit should be aimed at putting the increase in as good a light as possible. For example, we should make clear that in setting cash limits, the Defence programme was still receiving higher priority than civil programmes. Moreover, we could still show that in cash terms the Defence budget was growing this year by nearly 3%, though she acknowledged that Mr. Pym had always talked about the commitment to 3% growth in volume terms.

/I am sending

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- 3 -

I am sending copies of this letter to Martin Hall (Treasury)
and David Wright (Cabinet Office).

Yours ever,

Alfred W. H. H. H.

B.M. Norbury, Esq.

SECRET

1 1/2% to be no less
 21.8% - with limit
 for last year



MO 8/2/12

The Chancellor will mention this
 briefly under Parliamentary Affairs -
 these because of the need to
 announce the increase in the cash
 limit by a written answer before the
 House sits.

PRIME MINISTERDEFENCE CASH LIMITS 1980/81

fact
 6.000.000

The Chancellor of the Exchequer will, I understand, be reporting to Cabinet tomorrow that he has agreed that I should be granted a net increase above my cash limits in the current year of £150M. I thought that I should set out, for the information of the Cabinet, the implications of this.

2. When cash limits for 1980/81 were established it was agreed that their application to Defence should be reviewed "in the light of developments in the international situation and NATO's response to them". This agreement enabled us to maintain to NATO and domestically that we were carrying out our declared policy (Command 7841) of increasing Defence expenditure in line with the agreed NATO aim of annual increases of in the region of 3% in real terms. The Defence Programme was constructed accordingly after discussion in the Defence and Overseas Policy Committee (OD). The increase of £150M will mean that, depending on the movement in prices during the remainder of the year, real defence will rise by rather less than 1½% in real terms, and not by the 3½% planned. I have accepted that this should be the case in the shorter term in the light of the very grave financial situation facing the country and the priority we must accord to getting the economy right. I would like, however, to explain the consequences of this for the Defence Programme in the current year and explain why I consider that this reduction must be limited to this year.

3. As regards 1980/81 there can be no doubt that the operational efficiency of the Forces will be impaired, there will be damage to Service morale and there will be an adverse effect on defence Industries. Unless very carefully handled there could also be difficulty in the party. I cannot yet explain in detail the measures I will have to take to contain the budget within the new limit but in broad terms they are likely to be as at Annex.

SECRET



4. If we were to continue beyond 1980/81 to fail to reach a 3% annual increase in real terms the consequences would be very serious indeed. There would be grave damage to the Defence Programme, for which my plans are now based, with OD's approval, on the assumption of a 3% increase; to our credibility in Parliament and in the country given the very positive line we have taken on defence since we came to power; and to the Alliance to whom we have already given a much needed lead and whose efficiency of working we were hoping to begin to improve. It is in the interest of getting things right in the longer term that I have agreed, albeit with the greatest reluctance, that we cannot reach 3% in the shorter term.

5. I am sending copies of this minute to other members of the Cabinet, the Minister of Transport and the Chief Whip; and to Sir Robert Armstrong. In view of its sensitivity I would ask that they limit strictly any further circulation.

Handwritten signature

Ministry of Defence

6th August 1980

MEASURES NEEDED TO FIND A FURTHER £250M SAVING IN THE
DEFENCE BUDGET IN 1980/81

Action already taken

Cuts of £250M in the defence programme have already been made in order to compensate for the faster than expected rate of progress on the defence equipment programme this year, in itself a result of the economic recession. A moratorium is being placed on new defence contracts (save for a few essential exceptions) in order to protect the programme against further unplanned growth this year. The moratorium, initially for three months, will last until further notice. If enforced for the whole year it might produce savings of at most £150M.

2. In addition nearly all works services have been stopped; all civilian recruitment halted except for scarce skills and young apprentices; schemes eg Assisted House Purchase for improving conditions of service have been deferred; and a number of Service exercises cancelled.

Action now required

3. In order to achieve the reductions now necessary to stay within the revised cash limit cuts will be made in a number of areas including stopping or cutting back hard on:

- a. training, and remaining exercises - up to perhaps £10M;
- b. personnel movements and freight - up to £30M;
- c. recruitment to the three Services - up to perhaps £30M.

4. Beyond this savings must come from among the following:

- a. fuel purchases for the RN - £40M could be saved by restricting the Fleet to essential trials and training, by withdrawing from NATO and other exercises, withdrawing the Belize guardship and cancelling planned overseas deployments. Further cuts would put fishery protection and Northern Ireland patrols at risk;

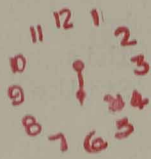
b. fuel purchases for the RAF. £50M could be saved by cutting flying by about one third. This would hit hard the operational capability of Strike Command and the Air Transport Force;

c. heating of domestic, administrative and technical accommodation - perhaps £50M;

d. stopping all uncommitted expenditure in the R&D area, drastically reducing purchases of accommodation stores and deferring expenditure in the nuclear field - up to £50M.

5. It would not make sense to go to the limit under any of these options: we shall have to find the most sensible combination of the measures but deep and conspicuous cuts in Service activity will be unavoidable.

- 6 AUG 1980



1. The first purchases for the MAF...
would be made by about the third...
would be made by the operational capability...
to be made by the Air Force...

2. The matter of domestic...
technical accommodation - perhaps...

3. The matter of...
the MAF...
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4. It would not make sense to...
of these... we shall have to...
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CONTRACTOR

CONFIDENTIAL



MINISTRY OF DEFENCE
MAIN BUILDING WHITEHALL LONDON SW1
Telephone 01-~~XXXXXX~~ 218 2111/3

MO 8/2/12

6th August 1980

Dear John,

R

DEFENCE EXPENDITURE 1980/81

4/8/80
42

At the Prime Minister's meeting yesterday I understand that the Chancellor suggested that up to £100m of defence expenditure could be saved this year by cutting works projects.

Mr Pym has asked me to say that this is not so. Heavy cuts have already been made in the works programme this year as part of the measures taken to contain the volume of the defence programme. Our estimate is that if all the remaining uncommitted works expenditure were stopped, excluding only essential maintenance, the saving would be less than a quarter of the figure quoted by the Chancellor. We shall be looking to make maximum savings within this figure under the moratorium on new defence commitments which Mr Pym plans to announce later this week. But some expenditure, for example on essential structural maintenance of existing buildings, will have to go ahead.

I am sending copies of this letter to Tim Lankester (No 10), Alistair Pirie (Chief Secretary's Office) and David Wright (Cabinet Office).

Yours and
Brian Norbury

(B M NORBURY)

A J Wiggins Esq
HM Treasury

CONFIDENTIAL

- 6 AUG 1980



MO 8/2/12

Understand F.P. will be
sent C.H..

MS.

CHANCELLOR OF THE EXCHEQUERDEFENCE EXPENDITURE 1980/81

I have been considering urgently the points put to me at the meeting held by the Prime Minister yesterday afternoon.

2. The proposition put forward was the defence cash limit should be increased by only £100M net - this would allow for a deduction of some £50M because of cash overspending in 1979/80. This would imply on the basis of present forecasts that I would need to reduce the programme by £300M. This would bring real growth down to below 1% as against the 3% aim. This reduction would be additional to the cuts in volume of £250M I have already made in the first 3 months of this financial year and others which I am likely to make to keep within my volume programme.

3. I know full well the economic problems which currently face the country as a whole and I am anxious to be as helpful as possible. Having looked again with the Chiefs of Staff at the programme I am reinforced in my view that your proposition if accepted would do great damage to our Defence effort, to relations with our Allies, to industry and to the confidence the Services have in the Government. I think too much is being asked of me and I need a little more help than is being proposed. If you for your part were prepared to accept that we should adjust the "fine" to take account of the fact that a significant part of my overspend arose from circumstances entirely outside our control (the loss of receipts from Iran) and that we must adopt a figure the consequences of which are defensible in terms of our public commitments to our Allies and to the Services themselves, I should myself be prepared to agree that in present economic circumstances we cannot fulfil in full the 3% aim for the present financial year. What I have in mind is that we should plan on the basis of an uplift of about £210M net to which would be added the small sum needed to meet a fine on the revised basis now proposed. A settlement on these lines would mean that I

would be accepting a volume squeeze of the sort anticipated at the time of the Budget in spite of our recognition then that defence was a special case. We should need to make clear that our failure to meet the 3% aim this year did not mean that we were not going to do so in future years. h

4. A settlement on this basis would still involve significant and damaging adjustments to the Defence Programme in the current year when taken alongside the measures needed to rein back on volume. I cannot tell you in detail what steps I shall have to take because they will have to be worked out and we shall have to talk to industry. I shall want to rein back our payments to industry and possibly introduce for our major contractors a monthly payments scheme. This may need to be imposed because of industry's cash flow problems which are a primary cause of defence problems. We shall have to go in a substantial way into the Services "activity" areas - this is not over-calling the hand, it is unavoidable. Exercises, training, sea-time and flying will all have to be curtailed and in some cases stopped. I am even having to consider extending the tour of units in Northern Ireland because we shall not be able to afford to bring them back this year, and whether we should cancel our major, and well publicised, NATO exercise Crusader 80. The cuts will go deep and cannot be concealed.

5. I can understand that you will want to make an announcement about cash limits this week. Presentation will be all important and it is essential that it should be low key. But complimentary to your announcement however, I should have to make public that I was reviewing the progress of expenditure on the defence programme and that the following decisions were likely to be necessary:

a. a moratorium, initially for 3 months, on the placing of new defence contracts (save for a few essential exceptions);

b. a decision not to proceed now with the purchase of either the Jetstream or the Beech aircraft;

c. a decision not to proceed with the purchase of 10 Sea Harrier aircraft;

d. a decision to delay the introduction of the scheme we have already approved for Assisted House Purchase for the Services;

e. a decision to continue the freeze on civil service recruitment for a further 3 month period though I would say that we intended to recruit 1800 apprentices (as compared with 2400 last year).

6. I think we recognise that we are having to take hard decisions now on the basis of incomplete information after only one Quarters' financial results. Given all the uncertainties, I hope you will find it possible to agree that the best broad compromise between the conflicting demands of policy would be to increase my cash limit as proposed in my third paragraph. Advice will have to be given to the Cabinet on Thursday and I should therefore be grateful for very early word.

7. I am sending copies of this minute to the Prime Minister; and to Sir Robert Armstrong.

78

Ministry of Defence

5th August 1980

CONFIDENTIAL

cc. HMT
DIT
CO

H8



Defence

10 DOWNING STREET

From the Private Secretary

5 August 1980

The Prime Minister has seen the Secretary of State for Defence's minute of 17 July following correspondence with Cranley Onslow about defence programmes. She has also seen the Secretary of State for Industry's comments of 4 August.

She agrees that it would be helpful if officials could quantify the financial effects in recent years of crediting the defence budget with the receipts in question.

I am sending copies of this letter to Martin Hall (H.M. Treasury), Ian Ellison (Department of Industry) and David Wright (Cabinet Office).

M. A. PATTISON

ARB

D.B. Omand, Esq.,
Ministry of Defence.

CONFIDENTIAL



CONFIDENTIAL

Prime Minister

PRIME MINISTER

DEFENCE PROCUREMENT

Yes ~~not~~

These exchanges follow your correspondence with Cranley Onslow. Content to commission work by officials as at "x"?

MAP 4/8

I have read with great interest the minute of 17 July to you from the Secretary of State for Defence concerning his discussion with Cranley Onslow on defence procurement matters.

2 The question of R&D levies on defence sales seems to me to be of relevance in the context of public purchasing policy.

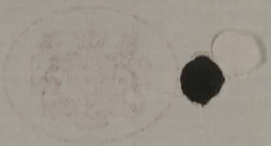
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I would find it helpful, therefore, if officials could be invited to quantify for us the financial effects in recent years of crediting the defence budget with such receipts.

3 I am copying this to Francis Pym and the other recipients of his minute.

K.J.

K J
4 August 1980



- 4 AUG 1980

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SUBJECT



File

10 DOWNING STREET

From the Private Secretary

4 August 1980

Dear Martin,

The Prime Minister held a meeting this afternoon with the Chancellor, the Secretary of State for Defence and the Chief Secretary to discuss the defence budget and the problem of this year's cash limit over-spend. Sir Anthony Rawlinson, Sir Frank Cooper and Sir Robert Armstrong were also present. They had before them as background the Chief Secretary's minute of 30 July and the note by Treasury and Ministry of Defence officials enclosed with it setting out the factual position.

The Prime Minister said that she understood that defence spending in 1980/81 was projected to exceed the cash limit by £650 million. £250 million of this was due to volume over-spend, and the Ministry of Defence were apparently taking steps to eliminate this. The remaining £400 million was due to pay and prices being higher than the assumptions made when cash limits were set. There was no way in which it would be possible to meet this £400 million over-run. Compared with other Departments, the Ministry of Defence had already been favourably treated. They had received a cash limit increase to cover the additional costs of the Armed Forces Pay Review Body's recommendations; they had been allowed to retain the savings from the Civil Service cuts. They had also benefited from the appreciation of sterling. Despite all this, defence spending was running well outside the cash limit while other Departments were expected to stay within theirs. The extent of the over-spend was aggravated by the pay settlement just completed for the Civil Service industrials, which had been extremely generous. If the Ministry of Defence had fought harder to keep this settlement down, they would not be in such difficulty now. Against the background of very heavy Central Government borrowing in the first quarter and the continued pressure on the private sector, she could not see how more than a small adjustment to the existing Ministry of Defence cash limit would be possible.

The Chancellor said that the latest internal forecasts showed the PSBR running at a considerably higher level in 1980/81 compared with the forecast made at the time of the Budget. There were a number of reasons for this, including excess borrowing by the local authorities and by the nationalised industries. But the Ministry of Defence over-spend was also an important factor, and there was growing concern amongst economic commentators and in the City that the Government was losing control. Other Departments were having to accept a volume squeeze through sticking to their cash limits, and he had no option but to ask the Ministry of Defence to do the same.

/The Chief Secretary

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- 2 -

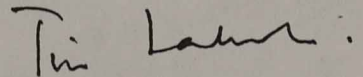
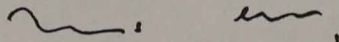
The Chief Secretary added that the Treasury were also looking for a deduction from this year's cash limit for the amount over-spent last year. Sir Anthony Rawlinson explained that, although an over-spend figure of £61 million had been mentioned, it might be possible to reduce the deduction to about £50 million because of additional receipts which had come to light.

The Secretary of State for Defence said that he accepted the principle of a deduction for last year's over-spend, and he also recognised the general economic case for restricting Government borrowing and spending. But the proposition that defence spending should stay within the existing cash limit had very important implications, which he would need to consider carefully. In effect, the Treasury were saying there could be little or no volume growth in defence spending this year. He had tried to be helpful to the Chancellor when the volume figures for this and subsequent years were set, and also when the cash limit was negotiated. But the Chancellor was now asking him to go a great deal further. Because so much of the programme was already committed, staying within the cash limit would require some very drastic measures, and it would be bound to cause trouble with our NATO allies. Moreover, if there was to be little or no growth in real terms for this year, how could he be sure that there would be any growth in future years? A decision to hold back defence spending this year would undermine the planning base for spending in the years ahead.

The Prime Minister suggested that the Treasury should agree an increase in the cash limit of £100 million net, or about £150 million gross including the deduction for last year's over-spend. She very much hoped that Treasury Ministers and the Secretary of State for Defence would be able to agree on this with a view to an announcement later this week. If it could be agreed, then the Chancellor could simply report the matter to Cabinet on Thursday. If no agreement could be reached, then the issue would have to go to Cabinet.

I am sending a copy of this letter to Brian Norbury (Ministry of Defence), Alistair Pirie (Chief Secretary's Office) and David Wright (Cabinet Office).

M. A. Hall, Esq., M.V.O.,
H.M. Treasury.



CONFIDENTIAL

SECRET



10 DOWNING STREET

From the Private Secretary

1 August 1980

sub
BF for mby Monday
10
File *sub*
b.c. Sir Robert Amichay
10
Mr Kerr.

The Prime Minister held a meeting this morning with the Chancellor and the Chief Secretary to discuss the defence budget and the problem of this year's overspend. Sir Anthony Rawlinson, Mr. Hansford and Mr. Kerr were also present. They had before them the Chief Secretary's minute of 30 July and the further note which you enclosed with your letter of 31 July.

The Chancellor explained that defence expenditure in 1980/81 was projected to exceed the cash limit by £650 million if no countervailing action were taken. £250 million of this was due to volume overspend, the rest due to pay and prices being higher than the assumptions made when cash limits were set. MOD were starting to take action to rein back the £250 million volume overspend but were doing nothing to eliminate the remaining £400 million. The Treasury would like to insist on the £400 million being eliminated too so that spending stayed within the cash limit. In addition, they wanted a deduction of £60 million to compensate for the MOD overspend in 1979/80. Other Departments were having to live within their cash limits and accept a volume squeeze; the MOD had been more favourably treated when cash limits were set and had been allowed to "keep" the cash from their staff savings; and it was crucial for the Government's borrowing plans and for the integrity of the cash limit system that MOD should not be allowed to overspend. The bad banking figures coming out the following week made it all the more important to act quickly and decisively. However, it was clear that to insist on MOD's staying within the cash limit (with the £60 million deduction on top) would be difficult. Annex D of the paper enclosed with the Chief Secretary's minute overstated the difficulties for the defence programme which this would involve; but they were none the less considerable.

The Prime Minister said that she was in full agreement with the Chancellor's objective but she felt an element of compromise would be necessary. After some discussion of the volume figures underlying the cash limits especially in relation to the NATO target, she suggested that the Treasury should be prepared to concede an additional £100 million after deducting the overspend for 1979/80 (i.e. about £150 million gross).

/The Chancellor

SECRET

SECRET

- 2 -

The Chancellor said this could be presented to the Defence Secretary on the following basis:

- (i) a £100 million reduction would ensure that defence expenditure rose 3% in volume terms compared with the 1979/80 out-turn;
- (ii) a further £200 million reduction was justified to bring the volume of spending back to what had originally been implied when the cash limit was set;
- (iii) the £150 million concession in gross terms still meant that MOD were being treated more favourably than other Departments.

It would be important, in addition, to insist that:

- (i) MOD should keep within the revised figure and not overspend as they had done in the last two years;
- (ii) there should be the deduction for last year's overspend;
- (iii) there should be no further review let-out;
- (iv) there should be no concession or commitment in respect of spending for later years (which was the subject of separate discussions between Mr. Biffen and Mr. Pym).

The Prime Minister will now have a meeting with the Chancellor, the Chief Secretary and the Secretary of State for Defence at 2.30 p.m. on Monday with a view to achieving a settlement on the above basis. You will be letting me have speaking notes, and an aide memoire on the figuring, for the Prime Minister's use.

I am sending a copy of this letter to Alastair Pirie (Chief Secretary's Office).

[Handwritten signature]

Tim Laker.

John Wiggins, Esq.,
HM Treasury.

SECRET

CONFIDENTIAL



Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

1 August 1980

C.A. Whitmore, Esq.,
No.10, Downing Street

Dear Clive,

DEFENCE CASH LIMITS

Following this morning's meeting, I understand that you asked that a draft speaking note, and some supporting material, should be prepared for the Prime Minister's use at the meeting with the Defence Secretary which has now been ... arranged for Monday afternoon. I attach the required papers.

Yours ever

John Wiggins

A.J. WIGGINS

DRAFT SPEAKING NOTE

1. The essentials of the situation described in the Chief Secretary's minute, and the paper by officials, are simple:-

Defence are on course to overspend their volume programme.

This is clearly unacceptable, and Defence have agreed to prune all excess volume growth.

But Defence maintain that they must achieve the agreed volume programme, whatever its cost.

The cost seems likely to be some £400 million above the cash limit, and Defence have bid for the extra cash, which would give them a 4% increase on last year's outturn.

Meanwhile, as the markets have spotted, they continue to spend at a rate which assumes acceptance of their bid.

But the Treasury reject the bid: hence this meeting.

2. To accommodate the bid would presumably entail:-

An addition to the PSBR, and/or

Cuts in other expenditure programmes, and/or

Increases in taxes.

Realistically, fiscal action is hardly possible. Nor are compensating cuts in other programmes. And the markets are looking for action to keep spending in line with the target for the PSBR, not to increase it. Holding down public

expenditure, and hence the PSBR, is crucial to the achievement of the economic strategy.

3. The Defence bid cannot therefore be accepted. Cash must rule, and be seen to rule. The volume of Defence purchasing must be brought down to what the cash limits will allow; and the sooner the markets see this happening, the better. Some modest increase in the cash limit need not be excluded, although Defence will have to accept a deduction to compensate for their overspend last year. [See Annexes] But an extra £400 million is just not on - nor is it needed to ensure that we maintain a respectable record in relation to the NATO target. Moreover, we interpret the NATO target in terms of outturn on outturn, not outturn on plans, and it specifically recognised that economic circumstances would affect what individual countries could achieve. Ours must affect what we can do this year.

4. Of course it will not be easy to bring spending back in line with the cash limits, perhaps marginally increased. But the MOD Annex to the paper by officials exaggerates the difficulties. Defence benefits from:-

A cash limit increase (£54 million) to cover the additional costs of the Armed Forces Pay Review Body's recommendations.

Retention of savings (£30 million) from Civil Service cuts.

The appreciation of sterling.

Increased receipts from Hong Kong.

- and some reductions in stock and on the works and equipment programmes should be possible without effect on the readiness of units declared to NATO, or their availability for exercises and routine activities. (The Annex is "horror comic stuff".)

5. A settlement must be announced before the House rises.

It must be:-

- In line with Cash Limits policy (ie incorporating the compensating deduction), and
- Consistent with the Government's rule that cash must determine expenditure, not vice versa.

It must also be:-

- Accepted as final (no more reviews), and
- Implemented with determination (no third consecutive overspend).

DEFENCE CASH LIMIT 1980-81

	£ million (cash)
Prospective overspend	650
Of which, volume excess over approved programme (Cmnd 7841) which Defence Secretary has agreed to eliminate:	250
Remainder, ie extra cash requirement arising from the excess of current pay (1) and price forecasts over those assumed in setting the cash limits:	400
A cash limit increase of <u>£400m</u> , restoring the programme in its entirety, would permit 4% real growth over the outturn in 1979-80.	
Amount required for 3% growth	300 ⁽²⁾
Reduction in programme implied by pay and price assumptions at the time of the Budget:	200
Remainder, ie extent of "unforeseen" squeeze	100
In addition, developments on the exchange rate, the contribution from the Government of Hong Kong, and civilian staff savings will make it easier for the MOD to absorb the squeeze.	

(1) Compensation has been agreed for Armed Forces' Pay (£54m) which has therefore been excluded from this calculation.

(2) Rounded.

DEFENCE BUDGET (1)

	1979-80	1980-81
Original cash limit	8005	10125
increases granted	549 ⁽²⁾	218 ⁽³⁾
Total	8554 ⁽⁴⁾	10343
Gross increase over previous year	24.3%	20.9%
Underlying growth ⁽⁵⁾ at constant September 1979 prices	2.4%	4.0%
The price forecasts at the time of the Budget implied that the cash limit would constrain growth to	....	2.2%
Current price forecasts imply that growth will be constrained to	....	0.3%
Growth which would be permitted by an increase in the cash limit of:		
£100m	....	1.25%
£150m	....	1.75%
£200m	....	2.25%

(1) The Defence Budget includes, in addition to the Defence cash limit, Service Pensions and certain other expenditure.

(2) Including £270m for Forces' pay, £100m for equipment and £140m compensation for VAT.

(3) £164m for Civil Service pay, and £54m for Forces' pay (not yet Voted).

(4) The outturn was £8615m.

(5) Defence Budget.

2/0
Tim Lashmer, No 10.



An extract from a recent minute
I put to the Chancellor. I hope we shall
put up something fuller on there
With the Compliments

of

Shirley

ADAM RIDLEY

Special Adviser

M 3717

Treasury Chambers,
Parliament Street,
S.W.1.

Mr Hansford judges (paragraph 2) that "MOD can justifiably claim (my underlining) that they could not now hold to the existing cash limit without taking measures which would be politically and militarily unacceptable". I must confess to grave scepticism about this view. While being aware of the difficulties facing any outsider in knowing how MOD works, I start from a presumption that this cannot be true, a presumption which is reinforced

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rather than reduced by the list of measures in Mr Hansford's Annex D. It says, "cuts of a further £450m would involve these measures". However this appears to be an almost preposterous list of sacred cows which are being offered for slaughter. One has only to leaf through the Defence estimates for a few minutes to notice some of the more glaringly obvious candidates for possible economies which are not mentioned. Such areas as the following could surely yield substantial extra savings if the will was there, and none of them is dealt with seriously in MOD's list:

	<u>Spending</u>	
	<u>Estimated 1980/81</u>	
Pay of Civilians	£1.048 bn	
Accommodation Services	£0.148 bn	Source:
Clothing, Textiles, Victuallery	£0.185 bn	Supply Estimates
Fuel and Utilities	£0.549 bn	1980/81
Lands and Buildings	£0.090 bn	
	<hr/>	
<u>TOTAL</u>	£2.020 bn	
	<hr/>	

A mere 2½% reduction in spending here is worth £40m or so. There is no discussion of a moratorium on civilian recruitment, only on recruitment of servicemen; no mention of disposals of buildings, land or stocks (this point is properly reflected in paragraph 3 of Annex C of Mr Kerr's minute); no mention at all of the part the dockyards or ordnance factories might be able to play.

One cannot study such options in depth outside MOD, but surely they can be expected to do so?

010
Working SECRET



Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000 } / July 1980

C A Whitmore Esq
Private Secretary
No.10 Downing Street
LONDON
SW1

R

Dear Mr. Whitmore

THE DEFENCE CASH LIMITS 1980/81

Following his talk with the Prime Minister this morning, and in preparation for tomorrow's meeting, the Chancellor has asked me to send you the attached note by Treasury officials on the possible scope for economy measures to avoid an increase in, or overspend on, the MOD cash limits in the current year.

Yours sincerely
David [Signature]

pp. A J WIGGINS

R

DEFENCE CASH LIMITS 1980-81

The main elements of the Defence Budget are:-

	<u>£ million</u>
Forces' pay	2.5
Forces' pensions (not cash-limited)	.5
Civilian pay	1.5
Equipment	4.3
Works	.7
Miscellaneous stores etc	1.2
	<u>10.8</u>

2. The scope for flexibility in these areas varies. On pay, both Service and civilian, savings could only be made by a full or partial ban on recruitment: the illustrative table at Annex A shows the effect of a 75% ban on each. Pensions do not enter into the reckoning. On equipment, it is estimated that about 5%, or £200 million will be uncommitted at this stage of the financial year. Works are a promising area, where there may be as much as £200 million still uncommitted. Then there are areas such as stores (total value £4 billion), training (which absorbs some £900 million a year in all) and fuel and utilities (£550 million a year) which clearly offer scope for economies, and on which economy cuts during the year traditionally fall.

3. That is the theoretical extent of flexibility. No doubt there are constraints on the extent to which stores can be run down or training cut without serious operational consequences. But it is implausible to suggest that the room for manoeuvre is severely limited even 4 months into the financial year.

4. In Annex D to the agreed paper by officials, the Ministry of Defence implied that flexibility would be minimal, and suggested that painful and highly visible cuts in service activity would be required if the cash limits were held. (The Annexes, unlike the paper, were not agreed between the two departments: Annex C set out the Treasury's view of the consequence of not holding the limits, and Annex D the Ministry of Defence's view of the consequences if they were held.)

It is unlikely that all the possible measures listed by the Ministry

of Defence are the ones which they would actually implement if no further cash were provided. For example, it is notable that the cuts are equally distributed between the three Services, and include no contribution from the civilian administration. And equal shares for the three Services would not in practice mean equal misery, since RN and RAF programmes contain a higher proportion of major projects, and therefore less room for manoeuvre than in the Army's programme, Army procurement being more diverse.

5. It would be for the Defence Secretary, in consultation with the Chiefs of Staff, to decide what economy measures should in fact be taken if £450 million had to be saved this year. That process has not yet taken place. The Treasury is in no position to attempt it. In Table 1 at Annex A we have nevertheless set out, for illustrative purposes, some areas in which we would expect MOD to look for economies. Cuts on the scale suggested in the works and equipment programmes (serials (a) and (b)) would not entail the cancellation of any existing contracts. The equipment programme cuts amount to some 1% of that programme in 1980/81. Given our estimate that some £200 million should still be uncommitted, our suggestion that a reduction of £35 million ought to be feasible may be over-conservative. No less conservative is our suggestion (serial (e)(i)) that reductions of £40 million might be possible through de-stocking. The stores inventories of the three Services comprise some three million separate items worth over £4,000 million. Implementation of the measures at serials (a) to (f)(i) would produce savings of £250 million.

6. The Treasury are not however able to say how far MOD plan to draw on such items for the savings necessary to effect the volume reduction to which they are already committed. There could be a risk of some double-counting, though the MOD Annex D suggests that it would be small in scale.

7. An alternative route for MOD would be to increase receipts. They are likely to receive additional receipts of some £10/20 million from Hong Kong during 1980/81, following the review of the Hong Kong Defence Costs Agreement. Larger sums might be found through more rapid disposals of surplus equipment, and surplus land and buildings
/ in the

in the Defence Estate. More than 15,000 married quarters are at present unoccupied. The Rayner review of the Bath PSA District identified scope for sales of land, and similar scope probably exists in other districts.

8. Even allowing for some increased receipts, cuts of the scale required if the cash limits were held would undoubtedly cause MOD some difficulty. There are however grounds for doubting whether the difficulties would be as great as the MOD Annex D suggested. Economies in the areas indicated at serials (a) to (e)(i) should have little or no effect on the readiness of units declared to NATO, or their availability for exercises and routine activities.

HM Treasury
31 July 1980

Annex A

TABLE 1

(a) Works Programme:	Moratorium on New Starts	£100m ⁽¹⁾
(b) Equipment Programme:	Deferment of Lower Priority New Orders and new R&D contracts involving expenditure in 1980/81	£35m ⁽²⁾
(c) Nuclear Programme:	Deferment of Purchases of Nuclear Materials	£6m ⁽³⁾
(d) Reduction of Travel, Training, Overtime:	(as implemented in 1979/80)	£30m
(e) Reduction of Stocks	(i) 1% reduction in Level of General Stocks held	£40m
	(ii) Temporary rundown of Naval Oil Stocks	£35m ⁽⁴⁾
(f) Recruitment Programme:	(i) Moratorium on Recruitment publicity	£4m ⁽⁵⁾
	(ii) Reduce Recruitment by 75%	
	(a) Servicemen	approx £150m ⁽⁶⁾
	(b) Civil Servants	approx £50m ⁽⁷⁾

(1) Moratorium only on New Works in UK from August. Treasury figure represents some 50% of total expected expenditure on New Starts over the full financial year.

(2) MOD calculate that savings of £73m on procurement (ie excluding R&D) are feasible, but would be damaging. Figure therefore assumes only 50% saving from deferment of lower priority new orders.

(3) Assumes no deferment of purchase of materials necessary for Chevaline programme, and deferment of 50% of other proposed purchases.

(4) MOD calculate that £69m could be saved by making no further RN oil purchases in 1980/81, but maintain that this would mean that stocks would run out. Figure assumes only 50% reduction in expected purchases.

(5) 50% of intended 1980/81 provision.

(6) This would involve a 7½% cut in Service strengths.

(7) This would involve a 7% cut in MOD civil servants.

31 JUL 1980

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9 8 7 6

PRIME MINISTER

Meeting with the Chancellor on Thursday 31 July at 0900

I think you will wish to spend most of the meeting discussing the attached paper on the Defence cash limits problem. The Chief Secretary has, in effect, thrown the problem at you - since he has not offered Defence any compromise at this stage. However, I understand that Treasury officials believe it is quite impossible - and this is brought out in Annex D - to stick absolutely to the existing cash limits. Some compromise seems almost inevitable. But any concession is going to need very careful presentation in view of the level of borrowing over the last three months. The bad money supply figures which we are told will be coming out next week (the Treasury tell me it is likely to be 4-5% including re-intermediation) make it all the more difficult. The Treasury would like a decision and an announcement, if possible, before Tuesday's banking figures. But I do not see how this will be possible since any increase in the cash limit will have to be a call on the contingency reserve and, given the likely amount, this will have to go to Cabinet next week.

Mr. Biffen has suggested that you meet Mr. Pym and the Chancellor and himself. You may, however, want to sound out Mr. Pym on his own first. I think we will need to set up the meeting(s) for Friday.

The Chancellor may also want to raise the problem of BGC asset sales. As you know, Mr. Howell and, more particularly, Denis Rooke have been resisting the sale of the Wytch Farm oil field. The argument continues.

12

30 July 1980



PRIME MINISTER

DEFENCE CASH LIMITS 1980-81

As you know, I have been discussing with the Secretary of State for Defence the acceleration in the rate of defence spending which has taken place during the first three months of this year, and which could lead to a substantial overspend on his cash limits if the present trend continues and no corrective measures are taken now.

2. Whereas we have defined the problem in our discussions, we have not been able to agree on the solution, since it involves a conflict between two important objectives of Government policy. But we agree that the conflict must be resolved quickly. I think therefore that the next step would be for us to have an early talk with you and the Chancellor with a view to reaching a solution which we might ask Cabinet to ratify.

3. As background for this discussion, I attach a paper, agreed at official level between the Treasury and the Ministry of Defence, which describes the problem and sets out the position of the two Departments.

4. The crux of the matter is that if the Defence cash limits are held to their present levels without adjustment, significant cuts will have to be made in the defence programme and there will be virtually no growth on last year's outturn. The Defence Secretary tells me that, as well as being militarily damaging, the cuts will be visible and are bound to lead to criticism at home and from our Allies. To restore the 1980-81 programme to the level planned in Cmnd 7841 would require an increase in the cash limits of around

£400m. I have established that an increase of some £300m would be sufficient to allow 3% growth on last year's outturn. But, as I explained to the Defence Secretary, an increase of £300m would lead to a corresponding increase in the PSBR, and this would endanger the successful achievement of our economic and financial policies. The danger would grow if other major spending Departments - none of whom are at present threatening to overspend - were to conclude that we were moving to a more liberal cash limits regime. The nationalised industries and local authorities would also take note.

5. To resolve this dilemma we need to find a formula which can serve two purposes. On the one hand, the Secretary of State looks for an increase in the volume of Defence spending this year: it is a matter of judgment what figure he could represent as a reasonable discharge of our obligation to NATO in a year of great economic difficulty. If the Secretary of State's position is sustained, UK's Defence spending this year would (on the NATO definition) be 4.0% higher in real terms than it was last year. This compares with planned increases of 3.3% in the US, 3.0% in France, 2.7% in West Germany and 2.2% in the Netherlands; and with planned reductions of 1.4% in Italy and 2.0% in Belgium. On the other hand, I am clear that I could not concede an increase of as much as £400m, or anything remotely approaching that figure, without jeopardising the achievement of our economic aims. To ensure that I can hold to the current policy on cash limits generally, if an increase has to be granted it must be much smaller than this, must be seen to be justified on grounds which are special to Defence, and must be a final settlement not subject to any further review.

6. The Defence Secretary and I believe that an early discussion with you and the Chancellor would help to resolve the dilemma and to produce such a formula. If you agree, you may wish to arrange an early meeting.

7. I am sending copies of this minute to the Chancellor and the Defence Secretary.

W J B

JOHN BIFFEN

DEFENCE CASH LIMITS 1980/81

NOTE BY HM TREASURY AND THE MINISTRY OF DEFENCE

The Cash Limit

1. Financial provision for the Defence Programme in 1980-81 was set at £7997m at 1979 Survey prices, and this figure was published in Cmnd 7841 in March. It was £65m below the figure first agreed, and published in Cmnd 7746 in November. In agreeing on the reduction, the Chancellor and the Defence Secretary also agreed that the resultant MOD cash limit should be increased to take account of the Spring Armed Forces Pay Award and, "should be subject to review in the light of economic and international circumstances, with a view to aiming for an increase in real terms in the region of 3% in line with the agreed NATO target". The terms of this agreement, which reflected the Defence Secretary's concern that the element of volume squeeze imposed by the cash limit should not be such as to make the NATO target unattainable in 1980-81, are attached at Annex A. There was no commitment on either side as to the action which might flow from a mid-year review.
2. The Defence cash limit was then set at £10,125m. This represented a mechanical, but mutually agreed, revaluation of the Survey figure on the basis of the standard inflation assumptions (14% for current expenditure on goods and services including pay). An increase of £50m has since been agreed to cover the additional costs of the April Armed Forces Pay Review Body recommendations. In addition, Defence's share of the central vote for Civil Service pay amounts to £163.8m.

The present forecast

3. The forecast of inflation (16½%) made at the time of the Budget in March implied that the cash limit assumption would impose a volume squeeze for the Defence Programme of £175m at 1980 Survey prices or £200m in cash terms. On the basis of the cash spent in the first quarter of 1980-81 defence expenditure is projected as likely to exceed the cash limit by about £650m if no countervailing action is taken. £250m of this would be volume in excess of the programme published in Cmnd 7841 and £400m would be due to pay and prices being higher than the assumptions made when the cash limit was fixed. In addition, in accordance with the normal principle, the Chief Secretary

/has

has proposed that the MOD's £60m cash limit overspend in 1979-80 must be deducted from the 1980-81 cash limit.

4. The risk of an overspend was immediately detected by MOD's internal control procedures and the Treasury's monitoring arrangements. The principal reasons have been established, although the figures are still provisional.

The reasons for the forecast overspend

5. The increased volume of expenditure reflects the economic climate. Firms short of other work are getting ahead with defence orders faster than planned; and to ease their cash flow and keep down their borrowing at a time of high interest rates they are sending in their bills more promptly than usual. Detailed analysis of the first quarter figures is not yet complete, but it is clear that volume has been running well ahead of plan. Contractual terms make it difficult and uneconomic for the Ministry of Defence to slow down the rate of payment on work which is under way. They are, however, determined to take the necessary steps to bring volume into line with the programme. Economy measures to effect a reduction of £150m have already been set in train and further measures to save the additional £100m are now being identified.

6. The Ministry of Defence's estimate of a £400m cash deficiency assumes inflation at a higher rate than allowed for in the Budget forecast. This is not markedly out of line with current forecasts for prices generally; the three month lag on payments for defence contracts delays the benefit to be derived from the expected deceleration of inflation in the second half of the financial year. The estimate takes account of the £60m net by which the Defence Budget is expected to benefit this year on account of movements in exchange rates since the cash limit was fixed. It also takes account of the additional flexibility on procurement which MOD enjoy through keeping savings (£30m in 1980-81) accruing from agreed reductions in Civil Service manpower.

Factors to be taken into account

7. The pay and price increase must be looked at in the light of the following factors:-

/(a) the primacy

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- (a) the primacy the Government attaches to maintaining the cash limits;
- (b) the agreement described in Annex A to keep the cash limit under review in the light of the economic and international situation with a view to aiming for an increase in the region of 3%;
- (c) the public statements of Ministers about the importance attached to improving British defences (examples in Annex B).

8. As Ministers recognised before Cmnd 7841 was published there is a conflict between the two objectives of constraining the volume programme to keep within the cash limits, in line with agreed Government policy, and the political commitment, undertaken by the Government, to aim at real increases in defence expenditure in the region of 3% per annum.

9. If the cash limit were not to be increased there would be the prospect of no real growth in 1980-81 over 1979-80, and perhaps even a slight decline. Without the deduction for last year's overspend the change would be + 0.3%, with it - 0.3% on the latest forecast of 1979-80 outturn.

Alternative courses

10. Given MOD's acceptance of the necessity of pruning volume growth to bring the programme back to the size envisaged in Cmnd 7841, the problem concerns only actual and forecast increases in pay and prices. The two main courses, and their consequences, are as follows:-

(a) to increase the MOD cash limit to eliminate volume squeeze, permit expenditure at the Cmnd 7841 level, and thus show an increase of over 3% compared to 1979-80. This would require an increase of £400m and no deduction for the overspend in the previous year. In the Treasury's view (see Annex C) such an increase would do grave damage to the economic strategy, and the credibility of cash limits;

(b) to allow no increase in the cash limit. Taking into account the compensating deduction for the 1979-80 cash limit overspend, MOD would be required to take additional economy measures

/sufficient

sufficient to generate reductions of a further £460m, in addition to the £250m already being found: a total of £710m. Given that 90% of its equipment expenditure is already committed by the start of the financial year; that cancelling contracts and introducing redundancies increases expenditure; and that the most obvious sources of economy have already been tapped for the £250m reductions to which MOD are committed, cuts of a further £460m would fall mainly on activity levels, ie operational training, exercises, and recruiting (see Annex D).

11. The choice between these two options is one for Ministers, who will wish to weigh the importance of holding the cash limits against the political need to demonstrate an increase in defence expenditure of over 3% this year. The choice must be faced now, because delay would enhance the practical difficulties of option (b) for MOD. The least desirable outcome, from all point of view, would be a delayed decision to hold the cash limits which resulted in MOD in fact overspending them for the third consecutive year.

ANNEX TO LETTER OF 30 JANUARY 1980 FROM THE PRIME MINISTER'S
PRINCIPAL PRIVATE SECRETARY TO THE PRIVATE SECRETARY TO THE
CHANCELLOR

DEFENCE BUDGET 1980/81-1983/84

The Ministry of Defence's cash limit for 1980/81:-

- i. will be raised as necessary to cover the cost of the Government's decisions on the recommendations of the Armed Forces Pay Review Body; and
- ii. will otherwise be on the same basis as the cash limits decided for other public expenditure programmes but subject to review in the light of economic and international circumstances, with a view to aiming for an increase in real terms of in the region of 3% in line with the agreed NATO target.

As a contribution towards the measures necessary for a major reduction in public expenditure in 1980/81, the Defence Secretary will carry out measures to achieve a reduction in defence spending of £62m. The planned figure of £8062m published in Cmnd 7746 for 1980/81 will be reduced to £8000m at 1979 Survey prices.

The figures for the later years, including provision for Polaris replacement costs, will be £8240m in 1981/82, £8487m in 1982/83 and £8742m in 1983/84.

PUBLIC STATEMENTS ABOUT DEFENCE SPENDINGElection Manifesto

"To strengthen Britain's defences and work with our Allies to protect our interests in an increasingly threatening world."

"We shall only be able to decide on the proper level of defence spending after consultation in Government with the Chiefs of Staff and our Allies. But it is already obvious that significant increases will be necessary. ... We will give our Servicemen decent living conditions, bring their pay up to full comparability with their civilian counterparts immediately and keep it there. In addition, we must maintain the efficiency of our reserve forces. We will improve their equipment, too, and hope to increase their strength."

NATO Defence Planning Committee Ministerial Meeting, May 1979

"On resources, we accept the call to aim at 3% real increases, naturally my Government hopes very much that every other Government will take the same view. We see very clearly the need to devote more resources to defence. My Government has not yet had time to review the public expenditure in our country, except that we know already that it is too high. We know that we have economic circumstances ahead of us that are difficult and that might affect what can be achieved, yet we accept that call to aim at a 3% increase in resources devoted to defence. In saying that, Chairman, I would like to say that of course we support the other important initiatives such as the Long Term Defence Programme which I have already mentioned. In conclusion, in saying that my Government approves this report, I just want to add that the United Kingdom, to the limits of its capability, wishes to play its full part in the absolutely crucial work that lies ahead for this Alliance." (Mr Pym).

Churchill Memorial Lecture by PM, Luxembourg, October 1979

"There is no need to match the sacrifices demanded of the Russian people. But can we match the resolve shown down the years by their leaders? Happily the Alliance is bestirring itself. The facts are becoming more widely acknowledged. NATO countries have agreed on a target of annual increases of 3% in defence expenditure. We British are prepared to meet that challenge. We look to our Allies to do likewise."

Statement on the Defence Estimates (Cmd 7826), April 1980

"defence cannot be turned on and off like a tap: reasonable continuity of policy and funding is essential The defence programme cannot be insulated from all change, but our aim is to restore its momentum and expand it in the ways we have described. This will mean increased defence spending. But we shall not feel obliged to adhere slavishly to a particular growth path, nor shall we consider it a failure of policy if we modify our spending plans in either direction from year to year as new information becomes available."

Letter from PM to President Carter, 10 July 1980

"In particular, I would like to assure you that the United Kingdom Government continues to give wholehearted support to the NATO Long Term Defence Programme and to other strengthening of conventional forces. The United Kingdom Government has substantially increased its defence spending, in accordance with the NATO's collective policy, and plans to make further such increases in future in order to improve the effectiveness of its all-round contribution to Allied deterrence and defence. In this regard the objective of the United Kingdom Government is to take advantage of the economies made possible by the cooperation of the United States in making the Trident 1 missile system available in order to reinforce its efforts to upgrade its conventional forces."

CONSEQUENCES OF INCREASING THE CASH LIMIT

As was noted in the Cabinet discussions on 3 and 10 July, it is crucial to the success of the macro-economic strategy that spending authorities stay within their cash limits. Unless expenditure is controlled within the limits this year there will be the greatest difficulty in securing an outturn for the public sector borrowing requirement in line with the Budget forecast of £8½ billion. If the PSBR could not be maintained there would be serious consequences for inflation, for interest rates and for confidence in the Government's policies generally: it might be necessary to take fiscal action to compensate for a substantial prospective overspend.

2. It is also of great importance to the financial strategy that the cash limits system should not be weakened. Cash limits discipline cannot be applied selectively: there would be a danger that any precedent would be followed by other spending departments. This could have the gravest consequences for the success of the medium term financial strategy, which necessarily depends on keeping public spending within whatever limits are laid down so that, among other things, public borrowing can be kept under control. Without success in that strategy for reducing inflation there can be no hope of restoring economic growth.

3. Ministers this year deliberately set the cash limits at a level which did not fully allow for expected inflation. They were intended to impose some volume squeeze. It is an essential principle of cash limits policy that cash limits, once set, should be adhered to. The Ministry of Defence is too important a part of central Government spending to be exempted from this rule.



10 DOWNING STREET

17 July 1980

From the Private Secretary

Dear David

The Prime Minister has now seen your Secretary of State's minute of 16 July, about the proposed purchase of the Jetstream in relation to the cash limit for 1980/81.

In the light of recent developments over the cash limit, the Prime Minister agrees that action on the proposed Jetstream purchase should be suspended pending settlement of the cash limit issue.

The Prime Minister has noted your Secretary of State's suggestion that the opportunity of this delay should be taken to look again at the alternatives open to us. She is prepared to look at any alternative, although she has expressed her doubt as to whether the defence budget has room for any replacement aircraft of this kind at present.

I am sending copies of this letter to the Private Secretaries to the members of E(EA) and to David Wright (Cabinet Office).

Yours ever

Mike Pattison

David Omand, Esq.,
Ministry of Defence

Mr Kerr
PPS PS/FST
PS/MST PS/MST(L)

Sir D. Wass

Sir A. Laurinson

→ Mr Hansford

Mr F. Butler

Mr Cardona

Mr Ridley

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262/270

MEASURES NEEDED TO KEEP WITHIN THE CASH LIMIT

1. Cuts of a further £450M would involve these measures:

(a) Royal Navy (£150M) - Over 90% of the 1980-81 programme is committed and savings of £150M could only be achieved by an immediate moratorium on all new equipment development and production contracts; (£17M), purchase of oil stocks (£69M), freight contracts (£11M), and Service recruitment (£5M). There would be an additional requirement to cancel some existing contracts. Fuel would probably run out in December. The Navy would have to spend the remainder of the year in harbour. The Naval Procurement programme would virtually come to a halt. Development on the new class of conventional submarines would be stopped, and the order for the SSN 16, declared as a firm intention by Ministers in Parliament less than two months ago, would not be placed.

(b) Army (£150M) - All except direct operational activity would cease, including training (£15M), all exercises including "Crusader" (£7M), Service and civilian recruiting (£34M) and movements (£20M). There would also have to be an embargo on all uncommitted expenditure in the equipment (£16M) and works (£22M) fields. Even

/ curtailment ...

curtailment of the Army programme to this extent would still leave them some £30M short of their £150M. To find the remainder, break clauses would have to be invoked in about one fifth of equipment contracts, resulting in cancellation charges next year and major disruption of the programme.

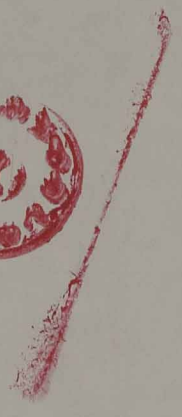
- (c) Royal Air Force (£150M) - Savings of £150M in the Air Force programme in 1980-81 could be achieved by grounding RAF aircraft not only for training, transport and movements purposes but also for operational flying. Other ways of reaching this total in whole or part would involve a ban on Service recruitment (£10M) and a moratorium on all air systems equipment requisitions (£40M) and most works projects (£35M); some of the latter are due to be part NATO funded and for every £35 we save we would lose £65 of NATO money. Ceasing civil charter, surface movements (£20M for the two) and turning off heating in domestic, administrative and technical accommodation (£45M) would also have to be considered.

2. The scope for short term savings in other areas of the defence programme is extremely limited. Substantial savings (£50M) could only be made by deferring the processing of certain nuclear materials, deferring the purchase of propulsion fuels from the USA (possibly contravening the UK/US agreement), and stopping all further uncommitted expenditure in the R & D area, and drastically reducing planned purchases of accommodation stores.

/ Some

3. Some measures of the kind described above may be needed to achieve the £100M savings now being identified to bring volume into line with the programme (see paragraph 5 of the paper).

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CR.

MO 26/2

PRIME MINISTER

DEFENCE PROCUREMENT

I saw Cranley Onslow on 7th July to discuss the points in his letter of 30th June to you and I have seen your letter to him of 7th July. — *no 2nd carbon*

2. Cranley's main concern is that the Government should buy as much defence equipment as possible from British firms and he made particular reference to the Infantry Fighting Vehicle (on which we have of course now announced a British solution) and to the AV8B (where the industrial arguments are in fact highly complex). I did not get onto the question of how we compare procurement costs of British and overseas defence equipment nor did I encourage him to think that there was much mileage in the idea of special transfer payments to Defence (his second point) in cases where British equipment is bought in preference to cheaper but equally acceptable foreign items.

3. On his third point about the R & D levy on defence sales I was able to tell him that the Defence Budget is in fact credited with the receipts from these levies. Apparently this point is not well understood in industry and although it is really an internal matter for the Government, I am putting this right. We did not spend much time on his fourth point. There is in fact already close consultation between my Department and the Department of Industry at both Ministerial and official levels.

4. As regards his fifth point, I welcomed the idea of engaging back-benchers in helping to promote defence sales overseas, but said I wished to think further about it. It could be useful. We shall need to avoid occasions when individual commercial interests might prejudice credibility and there will be occasions when it would certainly be wiser



for a visiting back-bencher not to become involved. But these do not seem unmanageable points.

5. On this basis Cranley seemed well content with our discussion.

6. I should I think add that we are receiving other approaches, in addition to Cranley's, on the question of how we compare the costs of satisfying Government requirements by purchase from British industry or from overseas. We were approached privately recently by some senior members of the Defence Industries Council on this point, and I know the Society of British Aerospace Companies are also concerned. In the case of defence equipment, they recognise that the MOD aim is to buy British unless there are overriding reasons of cost, performance or timescale which argue strongly to the contrary. They are also aware of our record with some 90% of our equipment budget spent with British industry on national or collaborative projects. They are, however, concerned at what they allege to be the basic approach of the economic Departments that in terms of employment and economic activity overall a pound spent overseas is the same as a pound spent in Britain and that straight cost comparisons should determine procurement decisions. They question the economics of this; they are concerned about the retention of industrial capabilities; and they do not believe any of our competitors behave in the same way.

7. I am not really in a position to comment on some of this and have not done so. But I wonder whether we do not need to give more thought to these issues or at least to engage manufacturing industry in a dialogue about them to clear up misunderstandings, perhaps on both sides.

8. I am sending copies of this minute to Geoffrey Howe, Keith Joseph, and John Nott, and to Sir Robert Armstrong.

Ministry of Defence

17th July 1980



Small, illegible handwritten mark or signature.

18 JUL 1960



Faint, illegible text covering the majority of the page, likely bleed-through from the reverse side.

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Treasury Chambers, Parliament Street, SW1P 3AG

01-233 3000 16 July 1980

C Whitmore Esq
Principal Private Secretary
Prime Minister's Office
No.10 Downing Street
LONDON SW1

Dear Clive,

DEFENCE EXPENDITURE

When the Chancellor calls on the Prime Minister tomorrow morning one of the subjects he will want to touch on is the problem of defence expenditure in the current year.

.... The Chancellor has asked me to send you the attached note by officials which he thinks the Prime Minister may find it useful to read. This follows on from the paper which the Chancellor left with her last week.

He has asked me to mention also two further points material to the present discussion of defence expenditure:-

(i) if no adjustment were made this year to take account of last year's £60 million cash limit overspend, the credibility of cash limits as a discipline would be severely weakened; and

(ii) unlike other Departments, the Ministry of Defence are not required to surrender the savings resulting from the progressive staff reductions planned over the period to 1983/84.

yours ever

John Wiggins

A J WIGGINS

DEFENCE EXPENDITURE

We cannot duck the problem we face over defence spending running ahead of the cash limit in the current year: it involves a clash of policies, and some practical problems too.

2. As a Government, we are committed to strict cash control. Our principal instrument is cash limits. It is crucial to the success of our policies for the PSBR that we hold the cash limits this year, and to the credibility of our control system that we are seen to do so.
3. We set the cash limits deliberately at a level which did not fully allow for expected inflation. They were intended to impose some volume squeeze. Most spending Ministers and Government Departments have accepted this, have pared their volume plans, and should be able to keep within their cash limits. (The problem of local authority overspending is as you know being actively pursued separately.)
4. The Ministry of Defence is the exception. Their spending in the first quarter of the financial year puts them on course for an overspend of at least £0.5 billion. Short of other orders, industry is working faster on theirs, with the result that they have been buying more volume than they expected. Some steps to bring the volume back to the agreed plan are now being taken. But on the provisional figures available, even to purchase the previously planned volume would entail an overspend on their cash limit of at least £0.4 billion. Prices being paid are several percentage points higher than forecast. Bills are being presented more quickly. Unlike other Departments, MOD are not paring their programme to match their cash but bidding for the extra cash.
5. We agreed in January that the cash limit should be reviewed during the year, without commitment to the outcome either way.
6. The MOD bid is now being examined by officials who will try to establish the precise scale of the problem and the measures that would be necessary to eliminate it. This work is as yet incomplete.

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We do not need to wait for all the details - indeed we cannot afford to. If we do not take early action it may not be possible to bring the rate of defence spending back within the cash limit in the current year. The practical problems of doing so are already great.

7. It is fundamental to cash limit policy that, in the current year, cash rules over volume. The crux is that MOD unlike other Departments decline to accept this primacy. They argue chiefly in terms of the NATO target. While some Allies interpret it as referring to 3% increases in cost terms, and others ignore it altogether, MOD interpret this in strict volume terms and attach cardinal importance to demonstrating that the planned increase in 1980-81 announced in Cmnd 7841 and the Defence White Paper is matched by a corresponding actual increase in volume outturn.

8. The NATO target is a broad political guideline, couched in suitably conditional terms and measured taking one year with another. It has helped to encourage the Alliance to put increased effort into defence to counter the threat from the Warsaw Pact. But it does not measure real defence effort: interpreted in volume terms it provides no incentive to efficiency and economy. It treats all defence expenditure equally, regardless of its cost-effectiveness.

9. This year we cannot both hold to the cash limits and accept MOD's interpretation of the NATO target. We must hold the limits. Unless financial discipline is maintained our economic strategy is in jeopardy. It is a sound economy which is the best basis for the UK's contribution to world security.

10. The longer the matter is unresolved, the greater the genuine difficulty MOD will have in paring their programme by the necessary amount.

Meeting with the Chancellor : 0900 hours Thursday 17 July

The Chancellor wants to discuss:

(i) The defence programme and how to handle the three outstanding issues - last year's overspend, this year's likely overspend and the Chief Secretary's proposal for a volume cut in spending over the next three years. I attach the note I did last week explaining this, and also the note the Chancellor handed you. *and a further note from the Chancellor* I am told that the review of this year's cash limit still is not completed; until it is, it will not be possible to take a decision. But I do think it would be worth focussing on what to do about the proposed volume cuts for 1981/82 onwards. The issue really is how we are to interpret the 3% NATO commitment. Mr. Pym will say that it has to be based on the 1978/79 out-turn; the Chancellor argues that we should take 1979/80 out-turn as the base, and he will argue that we should be interpreting the commitment in cost terms rather than volume terms anyway. ("Cost" in this context does not mean cash; it means the resources that are used in implementing a particular programme - taking into account the fact that the price of defence goods and services tends to go up more rapidly than the price of goods and services in the economy as a whole. By contrast, volume means the number of tanks, personnel etc.)

(ii) Comparability. The Chancellor will be circulating a paper on the outstanding comparability issues before the weekend - in particular, when to announce the demise of Clegg, what (if anything) to do about the review bodies and what to do about odd groups like the nurses. There is also the Chancellor of the Duchy's wish to announce in the Debate on Monday that MPs' pay and secretarial allowances will be subject to continuing annual review. The Chancellor wants to water this down, and I expect the matter will need to be discussed in Cabinet under Parliamentary. One further point:

/Clegg

Clegg has now submitted his general report (which I will put in the weekend box for you to look at); Mr. Prior is suggesting that it be published next week; I believe the Chancellor wants to delay until we have an announcement about the future of Clegg.

TL.

16 July 1980

Original a
Public Expenditure Pt 10

Prime Minister

Car PA 2



PRIME MINISTER

MS

The Treasury are giving Mr Pym
the option of an immediate
deduction from this year's cash
limit for last year's overspend
or wrapping this up in the
decision on the much bigger
question of the forecast overspend
for this year. No need for you
to take a view at this stage.
~~At~~ the Treasury are going ahead
with the PA2 idea.

CASH LIMITS

I must respond to the Defence Secretary's minute of 8 July.

PL

2. Let us first be clear about terms. There is no question
of excluding the possibility of an agreed policy decision to
increase a cash limit during the year. Obviously in present
circumstances there must be a strong presumption against such
increases, and grounds for considering them need to be compell-
ing. But where a spending Minister believes an increase necess-
ary and justified, it can be proposed. If Treasury Ministers
and the spending Ministers are unable to reach agreement, the
matter may have to be resolved collectively.

14/7

3. My minute of 3 July was concerned with overspending of cash
limits where no policy decision to increase has been agreed in
this way.

4. Here I am sure that we must maintain the general policy of
deducting the amount of any overspend in one year from the cash
limit for the next. I am glad to see that the Defence Secretary
does not object to this in principle.

5. I recognise the problems of the defence cash limit this year.
The facts are currently being sorted out by officials. When this
has been done I expect to be discussing the problems with the
Defence Secretary. I wrote to him (with a copy to you) on 9 July.
It remains my view that a deduction in respect of the overspend
last year should be agreed now. I should prefer that it also be

announced now, but if the Secretary of State prefers to include it in a later, more comprehensive announcement when we have settled the outcome of the wider review of this year's cash limit now in progress, I would go along with that.

6. The proposal that the PAC might investigate overspends (in the sense just discussed) where they involve a Supplementary Estimate, as well as those involving an Excess Vote (which the PAC already customarily investigate), should affect only a very few cases. It will be for the PAC themselves to decide whether to take up the idea, but if they do, it will be a minor, but appropriate and useful, reinforcement of the discipline of cash limits and of our commitment to proper control of expenditure.

7. The proposal has been the subject of correspondence between officials. Some initial criticisms were based in part on misunderstanding. In particular the C & AG has now agreed after discussion, that this is a proper area for the PAC.

8. The paper for the PAC has been amended to take account so far as possible of the comments made. I am sorry that the Defence Secretary still has reservations, but I have no doubt that the proposal is sensible and right. Since it is relevant to the PAC hearing on 16 July mentioned in my earlier minute, I have authorised the Treasury to put in the paper, and discuss it then with the PAC.

9. I am sending copies of this minute to members of the Cabinet and to the Minister of Transport, and to Sir Robert Armstrong.

W. J. B.

JOHN BIFFEN
14 July 1980

DEFENCE EXPENDITURE

*Tracy note handed
to the Ministry in
Chancellor 10/77*

Two objectives of Government policy are now in conflict: adherence to the NATO commitment, as interpreted by MOD, to 3% real increases in defence spending; and the need to hold cash limits, keep the borrowing requirement under control, and restrain future public expenditure plans. Defence accounts for 11 per cent of total public expenditure.

The NATO target

2. The Allies are asked to "aim at average annual increases in defence expenditure in the region of 3% in real terms". Only the UK, US and Italy did so in 1979, and only the UK, US, Germany, Netherlands, Norway and Canada have announced plans to do so over the period to 1983.

The UK interpretation of the target

3. We penalise ourselves by interpreting the target in volume, not cost terms. Few of the Allies do so. We thus take no credit for the major increases in forces' pay made in fulfilment of the commitment in the Manifesto (which was silent on the target). And since their primary concern is with the overall volume total, MOD have insufficient incentive to economise in administrative and support services and concentrate on front-line forces.

Implications for cash limits

4. Defence argue that it is insufficient to aim at the target: we must be able each year to demonstrate retrospectively that we hit it. But this year's cash limits were intended to impose some volume squeeze, and it is important for the CGBR that they be held. Officials are now reviewing MOD's current spending, and Defence are likely to bid for an addition of some £350 million to ensure 3% volume growth over the year (after the deduction - on which we must insist - of some £60 million to compensate for the overspend on the 1979-80 cash limit).

Implications for future expenditure plans

5. Defence expenditure was exempt from detailed scrutiny in the 1979 Survey. In view of the NATO target, it was accepted that we would plan

/ for

for 3% annual growth, and the debate centred on the baseline. The figures eventually agreed, and published in the White Papers, provided for a 3.6% increase in 1980-81, and 3% increases thereafter. (See attached table.) In the 1980 Survey documents the Chief Secretary has not challenged the 3% volume target, but has pointed out that annual average 3% growth over this year and the next three now calls for figures rather lower than those in the White Paper, because the 1979-80 volume outturn was lower than expected. Defence are in fact now asking for some £140 million in each of the three years 1981-82 to 1983-84 over and above what would be required to comply with the target, as they interpret it, and on the basis used in the White Papers. (See attached table.)

The case for a review

6. The importance of holding down public expenditure necessitates a review of our attitude to the target. NATO specifically accepted, when it was first adopted, that there would be derogations in difficult economic circumstances: the prospect of a 2½% decline in our GDP this year is highly relevant. The Defence White Paper pointed out that "we shall not feel obliged to adhere slavishly to a particular growth path, nor shall we consider it a failure of policy if we modify our spending plans in either direction from year to year as new information becomes available".

Options

7. Savings greater than those proposed by the Chief Secretary could be achieved if we were to come into line with the majority interpretation of the NATO target, or to conclude that our present circumstances necessitate a one-year derogation from it. Various courses are possible, depending on how far we decide to hold the cash limits this year. No increase in them would mean no volume growth, although we might still plan for 3% in future years.

Timing

8. It would be wrong to choose between the options until the current review of the MOD 1980-81 cash limit is complete, and bilateral discussions with other spending departments have established the likely feasibility of the Chief Secretary's Survey proposals. The proposal

/ in respect

in respect of defence is seen at this stage only as a marker. But it would be damaging in both the cash limits and Survey contexts, and to the search for economy, if Cabinet were now to accept that the MOD interpretation of the NATO target was sacrosanct. The case for demonstrating, in both plans and outturn, constant 3% volume growth in the defence programme does not necessarily take precedence over the Government's wider policy concerns and commitments.

Conclusions

- (i) Current financial and economic prospects necessitate a review of our current interpretation of the NATO target, and the re-assertion of the primacy of cash control over expenditure in the current year;
- (ii) public statements should be so framed as to impale us no further on the hook of our current interpretation of the NATO target; and
- (iii) decisions on future levels of defence expenditure should be deferred until later in the Survey.

DEFENCE PROGRAMME†

	1979-80	1980-81	1981-82	1982-83	1983-84
<u>£ million at 1979 Survey prices</u>					
The inherited plans (Cmnd 7439)	7917	8177	8219	8227	8227
(% increase over previous year)	5.9	3.3	0.5	0.1	0.0
June, 1979 Budget	+100	-115			
July Cabinet decision	-193				
Revised estimate of outturn	7824	8062			
Cmnd 7746 (November, 1979)	4.2	3.0			
(% increase over previous year)		-65	+21	+263	+513
January 1980 Cabinet decisions	-101				
Revised estimate of outturn	7723	7997	8240	8490	8740
Cmnd 7841 (March, 1980)	2.9	3.6	3.0	3.0	3.0
(% increase over previous year)					
<u>£ million at 1980 Survey prices</u>					
Cmnd 7841 revalued*	9288	9615	9941	10236	10540
(% increase over previous year)	2.9	3.5	3.4	3.0	3.0
Revised estimate/Cash Limits squeeze	-49	-175			
Estimating changes			+2	+5	+3
Survey baseline: Mr Pym's position	9239	9440 [∅]	9943	10241	10543
(% increase over previous year)	2.4	2.2	5.3	3.0	3.0
Chief Secretary's proposals			-139	-141	-143
(% increase over previous year)	9239	9440 [∅]	9804 [∅]	10100	10400
	2.4	2.2	3.9	3.0	3.0

+ The Defence Budget figures, to which the 3% strictly applies, are £3 or 4 million more in each year.

* and with some minor classification changes.

∅ The estimate of outturn in 1980-81 is uncertain: the Chief Secretary's proposal ignores the current year and bases 1981-82 on a 3% compound increase over 1979-80.

MEETING WITH THE CHANCELLOR AT 0900
THURSDAY 10 JULY

The Chancellor will want to go over the public expenditure papers for Cabinet. But he also wishes to discuss the particular problems of defence (though, as you know, Mr. Pym will not be attending Cabinet).

There are three issues:-

- (i) The £60 million over-spend in 1979/80, which the Treasury want to claw back by reducing this year's cash limit correspondingly. If they do not, so they argue, it will be patently unfair to other Departments who have over-spent and whose cash limits for this year are being reduced; and it will under-mine the cash limit system.
- (ii) The over-spend for this year which MOD are now forecasting. This apparently amounts to £550 million in total, of which about £400 million is due to inflation being higher than the cash limit assumed and £150 million due to an excess on volume. Mr. Pym is prepared to take corrective action to eliminate the volume over-spend, but is arguing for an extra £400 million to compensate him for the inflation element - relying on the review clause which was agreed when the cash limit was set.
- (iii) The volume cuts proposed by the Treasury amounting to £135 million in 1981/82 rising to £143 million in 1983/84. The Treasury argue for this on the grounds that it would maintain a volume growth rate of 3 per cent based on the 1979/80 out-turn, and ~~that~~ was some compensation for the higher projected cost of the defence programme relative to costs in the economy as a whole. (Expressed in terms of cost, the defence programme is expected to be £280 million more expensive in 1981/82 than the volume figures implied).

CONFIDENTIAL

- 2 -

Only the third issue is immediately relevant to tomorrow's Cabinet, and - particularly without Mr. Pym being present, it will not be possible to take a decision on it. But the Chancellor will want to reach decisions on the other two issues as soon as possible. For as Clive has explained, it is going to be very difficult - if not impossible - to pull this year's spending back by £550 million (or if you add the £60 million reduction for last year's over-spend, by £610 million). The sooner a decision is taken the greater will be the possibility of reining the programme back to the cash limit. But of course, Mr. Pym is going to resist this very strongly.

You clearly won't be able to reach a decision on the cash limit problem tomorrow; presumably you will have to have a meeting with Mr. Pym and the Chancellor separately or together when all the facts are known.

R.

P.S. See further papers which have just come in, in this folder.

9 July 1980

But I have had the Chancellor's Office text 'we don't want to spend too much time on the details of this tomorrow.'

CONFIDENTIAL



P. ... 2

As seen

Treasury Chambers, Parliament Street, SW1P 3AG

Rt Hon Francis Pym MC MP
 Secretary of State
 Ministry of Defence
 Main Building
 Whitehall
 London SW1A 2HB

9 July 1980

Dear Francis,

DEFENCE CASH LIMIT 1980/81

Thank you for your letter of 27 June.

Our officials are now carrying out a joint examination of the reasons for the upsurge in your spending this year. I am sure this should be completed quickly, and if possible a report submitted before the end of the month so that we can consider together what if any adjustment should be made to your cash limit.

I have to say however that any adjustment going beyond those elements we have already discussed would raise formidable difficulties for me. It is essential to uphold, and be seen to uphold, the principle that the Government contains its expenditure within the cash limits announced in the Budget. Any increase in your (or any other) cash limit would increase the PSBR and CGBR, with consequential effect on interest rates, unless it were matched by a corresponding reduction elsewhere in the spending plans, which at present I see no practicable way of achieving, or by an increase in taxation which would be highly damaging and would simply transfer the problem to the private sector. However, we need not cross that bridge until the report by officials is available.

We must however settle now, at least in principle, the issue of a deduction from the 1980/81 cash limit to compensate for the 1979/80 overspend. I note the objections you have raised to this course, but I cannot accept them. Our allies made no complaint when a similar deduction was made last year. The deferred Iranian receipts were but one small part of your total receipts which are always liable to fluctuate in either direction

during the course of a year. And whereas the forecast overspend of £60.2 million is provisional, it is the figure provided by your Department, and by far the largest, in absolute terms, of last year's overspends which are shortly to be announced.

The principle of deduction is important to our general stance on cash limits. It is essential to prevent a Department spending more over the two years than intended in cash terms. Failure to make the deduction would call in question the credibility of the cash limit system, to which we are as a Government firmly committed. The rules apply, and must be seen to apply, to all Departments. The fact that the proposed deduction is not greater than the amount of the overspend, eg to take account of inflation, could itself be a cause for criticism in some eyes.

In the light of these wider considerations, I hope that you will now accept in principle that the overspend should be deducted from this year's cash limit. The adjustment could be announced, with the other changes listed in my letter of 18 June, either immediately (which I should prefer) or when the review now in progress has been completed.

I am sending copies of this letter to the Prime Minister, Members of OD and Sir Robert Armstrong.

Yours
John Biffen

JOHN BIFFEN

Original a
Public Expenditure Pt 10



9

MO 8/2/12

PRIME MINISTERPUBLIC EXPENDITURE 1981/82 - 1983/84

I shall, as you know, be unable to attend Cabinet tomorrow. Had I been there, I would have been obliged to say that I cannot accept paragraph 14 of the Chief Secretary's paper, C(80)40.

2. We have only this week discussed in the Defence and Overseas Policy Committee (OD) ways of reshaping the defence programme to bring it into line with the last Public Expenditure White Paper (Cmnd 7841). Even taking account of the major economies in administration which I intend to secure, I have had to propose very considerable reductions in defence plans. The total reductions which I have made amount to £396M in 1981/82, £504M in 1982/83 and £568M in 1983/84.

3. The advice of the Chiefs of Staff has been made clear to OD. These reductions have no military justification. They act to lessen our security over the next few years at a time of mounting dangers and they bring us to the very edge of a crisis in our defence contribution to NATO. The reductions falling on British industry (90% of equipment bought by my Ministry is made in the UK) will cause serious difficulties, particularly in present economic conditions, for a number of firms both large and small.

4. I accepted these reductions in last year's Public Expenditure survey in the interests of our economic recovery. Our Allies were concerned that we were reducing expenditure below the plans left us by our predecessors but they accepted our good faith in our commitment to the Alliance and our determination to achieve the 3% real increases set out in our published PESC plans. Unrealistic cash limits frustrated our purpose last year when we underspent in volume terms (we achieved only a 2½% increase in our real defence effort, and even then there was a small overspend in cash as a result of the failure of Iranian orders). The Chief Secretary now



proposes that instead of making good this shortfall we should use it as a lower platform from which to calculate our 3% commitment. This is a transparent ploy which will fool no-one: we could not, as the Chief Secretary suggests, maintain that we are still meeting our obligations. We would not be believed, either by our friends abroad, or by the public and party at home. Neither will the lesson be lost on the Russians.

5. Our commitment as a Government to defence has become a vital anchor at a time of uncertainty and difficulty within the Atlantic Alliance. The cuts proposed by the Chief Secretary would take us over the safe limits of change.

6. At home I do not believe that further cuts in defence expenditure would be understood. The implications for industry would be very serious and we could see the disappearance of well-known names such as the Scott Lithgow and Cammell Laird shipyards as well as put in jeopardy the future viability of major elements of the aerospace and helicopter programmes. On the brink of a major recession it would be folly to inflict on industry damage of this magnitude.

7. I understand the reasons which have led the Chief Secretary to examine critically the public expenditure totals published in Cmnd 7841, but, as I made clear at OD yesterday, I believe that all the arguments point to sticking to our defence plans.

8. I am sending copies of this minute to our Cabinet colleagues, the Minister of Transport and the Chief Whip; and to Sir Robert Armstrong.

A handwritten signature, possibly 'R. J.', written in dark ink.

Ministry of Defence

9th July 1980

Original on Econ Pd
Public Expenditure
Pt 10



Prime Minister
with the defence cash
limit issue outstanding,
I doubt whether you
will want to respond
on the point in para 3.
As for the point in para 4,
I think we should await
the Treasury's comments.

MO 8/2/12

PM seen

T.

PRIME MINISTER

CASH LIMITS 1979/80

Flag A

The Chief Secretary minuted you on 3rd July, seeking agreement to the publication of a White Paper giving the provisional out-turn against cash limits in 1979/80. I have no objection to this.

T.
9/7

2. There are, however, two particular points in his minute on which I must comment.

3. The first is the statement that any overspend should result in a corresponding deduction in the following year, in order to avoid a higher total of spending over a longer period than we collectively planned. In so far as my Department is concerned, even with an estimated overspend of some £60m in 1979/80 we shall have achieved a volume increase in defence expenditure of only 2½% over the previous year, significantly less than the 3% increase which we collectively planned. A corresponding cut as a penalty in the current year would simply ensure that we fell short of our planned target again by a similar amount. I believe in cash control of expenditure, on the basis of taut but realistic limits which do not create unmanageable problems for Departments. Likewise I do not object in principle to the concept of a 'fine', particularly as I understand that Treasury are now prepared to contemplate a matching arrangement for carrying forward underspends. But any fine needs to be related to the circumstances.

But the same argument
best would
apply to
other programmes

T.

There is a
paper in
the cabinet
folder

T.

4. Second, the Chief Secretary floats in his minute the possibility that the Treasury might discuss with the PAC the possibility of the Committee investigating any breach of a cash limit, whether or not it formally involves the Treasury. His proposition involves



a considerable extension of the PAC role and could bring the Committee into conflict with the Departmental Committees. It would also seem likely to result in a PAC examination of issues which we ought to have settled among ourselves. I am told that there was some considerable criticism of the Treasury proposal when it was circulated at official level, not least from the C&AG himself. I think we need to look hard at this on the basis of a proper assessment of the pros and cons.

5. I am copying this minute to other members of Cabinet, to The Minister of Transport and to Sir Robert Armstrong.

78-
1

Ministry of Defence

8th July 1980

Onslow MP

(P)

Original in
Political office

7th July, 1980

Thank you very much for your letter of 30th
June.

I understand that you are having a meeting with
Francis Pym today, at which you will be discussing the
very important matters which you raise in your letter.

I have asked Francis to let me know the result
of your meeting with him.

I quite understand the reasons which prompted you
to write as you did.

MT

Cranley Onslow, Esq. M.P.
House of Commons,
Westminster, London SW1

c.c. The Right Honourable Francis Pym, M.C., M.P.



Jean Power Minister,

You may recall that when the officers of the Aviation Committee came to see you on May 13, I mentioned that we were hoping to frame some policy recommendations that would allow British industry to get greater benefits from Government expenditure on defence procurement.

We have now identified the following action as highly desirable : -

- i) the method of comparing procurement costs of UK and foreign defence equipment to be modified to take account of the overall economic advantages of purchases from domestic industry.
- ii) the Ministry of Defence to be allowed to claim appropriate credits on its budget whenever the application of this new cost comparison enables an order to be placed with British industry instead of overseas.
- iii) the proceeds of Government levies on defence sales to overseas buyers to be credited direct to the Ministry of Defence vote, instead of to the Consolidated Fund, and used to fund additional research and development projects.
- iv) the development of closer co-ordination between the Ministry of Defence and the Department of Industry at all levels, with the aim of creating a coherent strategy for British defence industry and maintaining a viable base for essential high technology.
- v) the involvement of Government back-benchers in the promotion of defence sales overseas, especially in the USA.

I realise these recommendations are very compressed, as I have set them out here. But I hope we shall have an early opportunity to expand upon them in discussion with Ministers at M.O.D. and D.O.I., as I am confident that they have wide support in British industry, and it is most important that action along these lines should be taken without delay.

Yours sincerely,
Cranley Onslow
Cranley Onslow.

Rt.Hon. Mrs.M.Thatcher, MP,
10 Downing Street,
London SW 1.

PRIME MINISTER

cc. Mr. Alexander

At your meeting with the Chancellor last Thursday, he mentioned the £400 million overspend on the defence programme for the first two months of this financial year. He also mentioned that he was considering the possibility of introducing cash rationing on a monthly basis.

I think it would be worth taking him up on this, and also asking him what other possible contingency action may be needed to ensure that the cash limits for the year are adhered to. With this in mind, I propose to write to the Treasury as per the attached letter. Agree? *Yes*

I should perhaps explain what is meant by MOD having overspent by £400 million in the first two months. There is no formal control on a month-by-month basis. But spending Departments are asked, before the financial year, to provide the Treasury with a profile of how they think the cash limit will be spent on a month-by-month basis. The Treasury then monitor actual spending against this profile. But if a Department is overspent compared with the profile, the Treasury cannot say that that Department is "breaking the cash limit". Hence the need to consider the possibility of monthly - or perhaps quarterly - cash control.

Finally, you should see the very worrying letter from the Defence Secretary at Flag A. When the MOD cash limit for 1980/81 was set, it was agreed - after much argument - that it would be "subject to review in the light of economic and international circumstances with a view to aiming for an increase in real terms of in the region of 3 per cent in line with the agreed N.A.T.O. target". This review will be completed in a few weeks' time, and I understand from the Treasury that MOD are likely to be asking for an additional

/ £700 million.

£700 million. Whatever the merits on defence grounds, it would create major problems if it were agreed - coming on top of the almost inevitable overspends on the nationalised industries cash limits and probably local authority spending too. If it begins to look as if Government spending and the borrowing requirement are going to overshoot significantly, then we really will be in trouble with the markets; and we could then find ourselves with another "gilts strike" of the kind we had last October. Put slightly differently, if we are to begin moving interest rates down in the near future, the risk that we will have to go into reverse and put MLR up again will be less, the more robust we are in making sure that the cash limits stick. If we seriously believe we are not going to be able to hold the borrowing requirement to the target level, then we should be all the more cautious in moving interest rates down.

On the other hand, we should not forget that lower interest rates ought to mean some relief for public spending. Not only is there direct spending on debt service; but with lower interest rates, the exchange rate will probably fall, and this will make British Steel and British Leyland more competitive, and thereby reduce the call on public funds. A lower pound would of course also reduce the pressure for spending ~~on~~^{or} other reliefs (e.g. reduced national insurance surcharge) in support of private sector industry.

R

We just can't afford that extra
now. It is indisputable

27 June 1980

to give a 16.5% increase for
wages on this basis. The
money is there. If it is taken out
that will be less for equipment. No

CONFIDENTIAL

MS



FILE

10 DOWNING STREET

From the Private Secretary

27 June 1980

When the Chancellor called on the Prime Minister last Thursday morning, they discussed briefly the reasons for the very large increase in spending in the first two months of this financial year compared with the first two months of last. The Chancellor explained that one of the main contributory factors was defence spending, which was £400 million more than expected.

The Chancellor went on to say that he was considering the possibility of introducing cash rationing on a monthly basis, or at any rate on a shorter timescale than the present 12 months basis. The Prime Minister would be grateful for a note on this when the Chancellor has reached his conclusions, and also on what other measures might be needed to ensure that this year's cash limits are adhered to.

T. P. LANKESTER

John Wiggins, Esq.,
H.M. Treasury.

CONFIDENTIAL

SB

B

CONFIDENTIAL



MINISTRY OF DEFENCE WHITEHALL LONDON SW1A 2HB

TELEPHONE 01-218 9000
DIRECT DIALLING 01-218 2111/3

MO 8/2/12

27th June 1980

W. H. Hester
Ronnie Minister

(2)

Ans 27/6

Dear John,

DEFENCE BUDGET

Thank you for your letters of 18th and 20th June.

As regards spending in the current year you have seen my letter to Geoffrey Howe of 18th June and you will know that I agreed with Geoffrey in specific terms at the beginning of this year when the 1980/81 figures were settled that there should be a review of the application to the defence budget of the cash limits agreed by the Cabinet with a view to aiming for an increase in real terms of in the region of 3% - in line with the agreed NATO target - an aim which Geoffrey himself confirmed during his budget speech.

Notwithstanding, therefore, the very real concern which we all share about the acute need to constrain public spending, what you suggest in your letters cannot be reconciled with the Government's carefully thought out defence policy and with what has been said consistently in public, and to our Allies since we took office. If the defence programme were to be contained as you have suggested within the current cash limit there would be no real growth, and indeed possibly even a real reduction. The cause of this difficulty is not difficult to see. Defence, unlike most other Departments, spends much of its resources on goods and services and not pay. On equipment for example, against an average inflation factor of 10½% in the cash limit the indications are that price increases will exceed this by between 3 and 7 percentage points. On oil alone we are now over £130M short of what is needed.

1

The Rt Hon John Biffen MP

CONFIDENTIAL



I must also express my doubt as to whether it would be physically possible to cut the defence programme so sharply and so quickly, even were I to agree in principle with what you propose. Creating redundancies and cancelling orders costs extra money in the short term. Attempting to comply with your request to contain expenditure within the current cash limit would mean, amongst other things, suspending all recruitment to the Armed Services; leaving ships, tanks and aircraft to stand idle and pulling out of NATO (and other) exercises and operations. It would negate all the goodwill we have achieved, destroy the painfully restored morale of the Armed Forces and precipitate a crisis of confidence within the Alliance, as well as in defence industry.

As regards last year's spending, it follows from what I have said that I am equally unable to agree to your suggestion that this year's cash limit will have to be reduced by the amount of last year's cash overspend, although I would again emphasise that I understand and share in the concern about the level of public expenditure overall. Defence spending in real terms last year fell well short of the original plan and, on top of that, is now forecast to have fallen by comparison with the estimate in Comnd. 7841: it now shows growth over 1979-80 of only 2.4% and not the 2.9% we have taken credit for in the House and in NATO. This will be difficult enough to explain to our allies but to accompany it by a statement that we are reducing this year's programme to "compensate" will seem extraordinary. You also overlook some of the elements which explain the overspending, notably that because of the consequences of the seizure of the US hostages in Iran, and the political decision not to resume business, receipt from arms sales to that country fell by £54M. If and when we finally get this money might be a better time to consider an offsetting reduction. Moreover the figure of £60.2M for the overspend is still provisional and there are a number of uncertainties yet to be resolved which could affect it substantially.

The next step must be for my officials to discuss urgently their calculations of defence cash flow and cash requirement for this year with yours.

I am sending copies of this letter to the Prime Minister, the members of OD and to Sir Robert Armstrong.

James
Francis Pym

Francis Pym

CONFIDENTIAL

Defence.



Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon Francis Pym MC MP
Secretary of State
Ministry of Defence
Main Building
Whitehall
London SW1A 2HB

FP
22/6
20 June 1980

Dear Secretary of State

DEFENCE CASH LIMITS 1980-81

Your minute of ~~18~~^{TVM} June to the Chancellor crossed with my letter of the same date. *with request of re.*

The adjustments to your cash limit which I described include an increase of £50 million for the cost of the Services pay settlement. This will ensure that the settlement is not at the expense of other parts of the defence programme.

I agree that our officials should jointly examine the reasons for the upsurge in your spending this year. This need not delay the announcement of the revised global cash limit of £10,276 million to reflect the four adjustments I listed in my letter.

Copies of this letter go to the Prime Minister and to Sir Robert Armstrong.

Yours sincerely

John Biffen

JB JOHN BIFFEN

[Approved by the Chief Secretary
and signed in his absence]

CONFIDENTIAL

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23 JUN 1980

PRIME MINISTER

MEETING WITH THE CHANCELLOR, 1230 PM FRIDAY 20 JUNE

This is your weekly meeting, which had to be postponed.

The Chancellor wishes to raise the following:

I Money supply and public expenditure

He has already warned you that the CGBR for the first quarter is likely to be very large. He also mentioned that Mr. Pym has put in for an increase in the defence cash limit. (This is not strictly true: Mr. Pym's minute at Flag A says that defence spending will not go up in real terms by 3% "unless there is an increase in the cash limit". But the implication is pretty clear.)

II Composite rate for the building societies

The Chancellor has minuted you at Flag B. A decision is apparently required before you go to Venice on a new composite rate. Under existing law, the rate ought to be increased from 21% to about 24% - because the average tax liability of building society investors has increased since the rate was last set four years ago. But an increase of this magnitude would almost certainly result in the building societies either putting up the mortgage rate or having to offer investors a lower interest rate. The Chancellor is proposing that the composite rate should only go up to 22½% this year, but this will require legislation which needs to be introduced on Monday. (It seems extraordinary that we have not been given more notice of this.)

III Handling of economic strategy discussion in Cabinet on 3 July

Robert Armstrong has written to Douglas Wass about this (Flag C); the Chancellor wants to discuss further.

19 June 1980

T.R.



Prime Minister 2

*See page 2
in particular.*

Treasury Chambers, Parliament Street, SW1P 3AG

B.

Rt Hon Francis Pym MC MP
Secretary of State
Ministry of Defence
Main Building
Whitehall
London SW1A 2HB

[Handwritten signature]

18 June 1980

Dear Francis,

DEFENCE CASH LIMITS 1979-80 AND 1980-81

The White Paper on the cash limits outturn for 1979-80 which we shall publish next month will show an overspend for the MOD 1979-80 global cash limit of £60.2 million. This overspend, although neither unexpected - the Spring Supplementary Estimates took total provision on the relevant Votes £63.8 million above the previously announced cash limits - nor unprecedented - the Defence 1978-79 cash limit was similarly overspent - is regrettable. It is clear that your cash limits for the current year will have to be correspondingly reduced. Parliament and public will expect this.

The change could conveniently be announced as part of a package containing three other adjustments to your cash limits which have, I understand, been agreed.

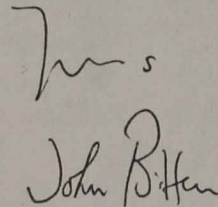
- (a) First, your share of the Civil Service Department's central vote for Civil Service pay, which is now to be distributed to Departments, amounts to £163.8 million.
- (b) Second, the Prime Minister told the House on 29 April that the Government accepted in full the recommendations of the Armed Forces Pay Review Body, that the consequences for the cash limit were being considered, and that an announcement would be made in due course. I understand that the implementation of the Award will cost £50 million more than the provision for Forces' pay in the Estimates.
- (c) Third, a small reduction in the cash limits need to be made to give effect to the agreed transfer of £2 million to the Foreign and Commonwealth Office for increased military training assistance.

The net result is that we need to announce that your global cash limit figure has been revised to £10,276 million. The elements in the calculation will have to be fully set out. If you agree our officials can discuss the terms of an announcement which should, in accordance with the normal policy on cash limit changes, be made as soon as possible, conceivably linked to the presentation on 24 June of the Revised Estimate for the Civil Service pay increase.

Meanwhile your Department's spending in the current year is a matter of great concern. Expenditure in April and May was £400 million more than expected, a third as much again as the usual proportionate spend in those months. If this were to continue, the prospect for 1980-81 would be of another overspend. This would be a third consecutive breach of the rules, and the second under this Government, and this time on a scale which would endanger our financial strategy.

As a Government we are firmly committed to the cash limit system. We are due to review your cash limits at some stage in the course of the year, but the results of that review should not be pre-empted by your proceeding on a course which would make it impossible to observe the present limits.

I am sending copies of this letter to the Prime Minister, members of OD, and the Secretary to the Cabinet.



JOHN BIFFEN



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MO 8/2/12

CHANCELLOR OF THE EXCHEQUERDEFENCE EXPENDITURE 1980/81

The first quarter of the financial year is now complete. The price rises that we have experienced so far, and those in prospect for the rest of the year, make clear we shall fall very far - and very obviously - short of the Government's objective of an increase in real defence expenditure in the region of 3% in line with the agreed NATO target unless there is an increase in the cash limit. Oil alone is already up by at least £130M.

2. This increase will need to go beyond the sum necessary to ensure that, as the Prime Minister said in the House of Commons on 29th April, the Services pay settlement is not at the expense of other parts of the defence programme.
3. It will clearly be necessary to look carefully into the figurework. I suggest that our officials should examine the problem together and make recommendations.
4. I am sending a copy of this minute to the Prime Minister and Sir Robert Armstrong.

Handwritten initials, possibly 'H.P.', in dark ink.

Ministry of Defence

18th June 1980

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5 4 3
1 2 1 0

18 JUN 1960

20

Defence

HOUSE OF COMMONS

Second Report from the

DEFENCE COMMITTEE

Session 1979-80

STATEMENT ON THE DEFENCE ESTIMATES 1980

Together with the Minutes of Proceedings
of the Committee; and the Minutes of
Evidence taken on 15, 16 and 17 April.

Ordered by the House of Commons
to be printed : 23 April 1980

The Defence Committee is appointed under S.O. No. 86A to examine the expenditure, administration and policy of the Ministry of Defence and associated public bodies, and similar matters within the responsibilities of the Secretary of State for Northern Ireland.

The Committee consists of a maximum of eleven Members, of whom the quorum is three. Unless the House otherwise orders, all Members nominated to the Committee continue to be members of it for the remainder of the Parliament.

The Committee has power:

- (a) to send for persons, papers and records, to sit notwithstanding any adjournment of the House, to adjourn from place to place, and to report from time to time;
- (b) to appoint persons with technical knowledge either to supply information which is not readily available or to elucidate matters of complexity within the Committee's order of reference.

The following were Members of the Committee when the Report was agreed to:

Sir John Langford-Holt (Chairman)

Sir Frederic Bennett
Mr. John Cartwright
Mr. Bernard Conlan
Mr. Bruce George
Rt. Hon. Dr. John Gilbert

Sir Timothy Kitson
Mr. Allen McKay
Mr. Michael Mates
Mr. Cranley Onslow
Mr. Patrick Wall

LIST OF WITNESSES

Tuesday 15 April 1980
AIR DEFENCE OF THE UNITED KINGDOM

Mr. J. Peters, Air Vice-Marshal P.B. Hine FBIM,
Air Commodore R. Colbeck (Ministry of Defence)

Wednesday 16 April 1980

PROCUREMENT

Mr. K.C. MacDonald, Mr. M. G. Power, Mr. A. W. Stephens,
Mr. J. Peters, Mr. W. Meakin, Mr. L. J. Rydill (Ministry of
Defence)

Wednesday 16 April 1980

MARITIME ENVIRONMENT

Mr. M. G. Power, Rear Admiral S.A.C. Cassels CBE,
Captain J.F. Woodward RN, Group Captain J.F. Willis (Ministry of
Defence)

Thursday 17 April 1980

SECRETARY OF STATE FOR DEFENCE

The Rt. Hon. Francis Pym, MC, MP

SECOND REPORT

The Defence Committee have agreed to the following Report:-

STATEMENT ON THE DEFENCE ESTIMATES 1980

Introduction

1. The Defence Committee have made a rapid inquiry into matters arising from the first full statement of the Government's defence policy embodied in "Defence in the 1980s", the annual Defence White Paper (Cmd. 7826). To meet the very tight timetable required, we met on three occasions on 15th and 16th April to take evidence from Ministry of Defence witnesses and on 17th April we concluded by taking evidence from the Rt. Hon. Francis Pym, M.C., M.P., Secretary of State for Defence. We have agreed our Report with unusual speed to ensure that it is available to the House for the debate on the White Paper. The White Paper was published on 2nd April, only two days before the Easter recess, and at one stage the debate on it was scheduled for the week after the Easter recess. We wish to stress that, in future, arrangements should ensure that the time which elapses between the publication of the White Paper and the debate on it should allow for a measured response by the Committee.

2. We took evidence in public from officials on three separate themes; air defence of the United Kingdom; procurement; and the maritime environment. In our concluding session we covered a wide range of defence policy with the Secretary of State. We held our meetings in public because we wish to provide as much information to the House and the public at large as is consistent with maintaining national security.

3. The White Paper is a more substantial document than has been published by successive Governments in recent years. There is always a balance to be struck between publishing a mass of sometimes indigestible material and producing a slim and readable volume which does not provide the amount of information which the House and the public have a right to expect. The first volume of this year's White Paper contains a great deal of material which is produced in a well written and well ordered form. A number of new diagrams and tables have been devised to illustrate points. This commendation is not intended to indicate that the White Paper is totally satisfactory. We hope that future White Papers will include details of unit costs of more weapons systems; total unit costs of systems including amortisation of Research and Development expenditure; further programme costs and full details of defence sales by contracts signed as well as by deliveries, details of which on their own may give misleading results. (1) Nonetheless what is now published represents an advance in style and content which we welcome. Moreover we acknowledge the readiness of Ministry officials to consider further improving some of the new material being published. (2)

1 Q.220-224

2 Q.103-5

Britain and NATO

4. The cornerstone of the policy of successive Governments since the War has been collective security through the Atlantic alliance. This alliance depends on the total commitment of all of its members to the acceptance of the principle that an attack on any member is an attack on every member of the alliance. The commitment is reaffirmed in the White Paper; and the scale of the forces and the growing inventory of sophisticated weapons of the Warsaw Pact reinforces its wisdom and necessity. While the relative superiority of the Warsaw Pact in conventional and nuclear armaments and forces must be, and is, viewed with concern, we welcome the Government's commitment to negotiate Mutual and Balanced Force Reductions (MBFR). Naturally, following recent extensive Soviet activity and in particular the invasion of Afghanistan, there is doubt about the value of arms control agreements with the Soviet Union. The statement of the Secretary of State that the Government would take every step to try to achieve better arms control through the Vienna MBFR talks is therefore the more welcome. (1)

5. As far as the Strategic Arms Limitation Talks (SALT) are concerned, the SALT II agreement currently awaiting ratification does not cover the systems of countries other than the United States and the Soviet Union. We have not investigated and do not seek here to comment upon the proposal to replace the Polaris force mentioned briefly in paragraph 211 of the White Paper. We are about to pursue an inquiry into this aspect of the Government's intentions.

6. Paragraph 305 of the White Paper affirms that Britain's military contribution to NATO is concentrated in four main areas: strategic nuclear forces; the Central Region of Europe; the Eastern Atlantic and Channel; and the defence of the United Kingdom home base. To meet these commitments, the United Kingdom maintains inter alia the British Army of the Rhine and eleven squadrons of Jaguar, Harrier, Buccaneer and Phantom aircraft in RAF Germany; the largest navy in Western Europe; forces to defend the United Kingdom against an attack; and supporting forces.

7. A number of defence analysts have suggested that the ever increasing costs both of modern weapon systems and highly trained personnel may lead to Britain having to review its defence policy. This could involve the adoption of a degree of specialisation in some aspects of defence and the abandonment of others. We note that in evidence the Secretary of State affirmed his intention to continue to fulfil the obligations currently undertaken but that within the context of the collective effort of the Alliance he would not rule out a change of British policy in the future. (1) Clearly the Government, having stated their policy in the White Paper, must be convinced of their capacity to carry it out. Nonetheless it is right that the policy should be assessed realistically in the future so as to ensure that resources are commensurate with commitments.

Wider Defence Interests

8. Following the increase of the capability and apparent determination of the Soviet Union to act on a world-wide scale, the Government have reviewed the ability of British Forces to act outside the NATO area in defence of British and Western interests. The Government, in the White Paper, affirm that the Services should be able to operate effectively outside the NATO area without diminishing the central commitment to the Alliance. (2) We note the intention of the Secretary of State to seek to anticipate the resulting operational requirements. (3) We accept his argument that it would be unwise to have a small standing force which in some situations would not be suited to the task in hand. (4) We agree that it would also be desirable to act in concert with the other Members of NATO. Having taken all of these factors into account, we must point out that the Government are seeking to assume wider responsibilities without adding any substantial extra resources. The only proposals to improve overall capability are listed in paragraph 409 of the White Paper and of these only the provision of additional transport aircraft was mentioned in evidence to us. We understand the Government's desire to be able to defend vital British interests outside the NATO area, but it must also be recognised that the performance of these tasks has to be grafted onto the four major British commitments, the resources for some of which are already severely stretched.

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- 1 Q423
 - 2 White Paper paragraph 409
 - 3 Q380
 - 4 Q381

Air Defence of the United Kingdom

9. Air Defence of the United Kingdom was the first of the subjects on which, in evidence, the Committee particularly concentrated their attention. (1) Paragraphs 341 and 342 of the White Paper state that this is an area in which there is room for improvement, and that plans are in hand to tackle the problem.

10. The United Kingdom has a crucial role in NATO planning as a main base for sea and air operations and as a source of, and staging area for, reinforcements for operations in Europe. Up to 40% of NATO's European air strength could be based here. (2) Over a million men and their equipment could pass through on their way from North America to the European theatre. The United Kingdom is also a base for longer-range theatre nuclear weapons at present carried in Vulcan and American F.111 bombers. This force will be supplemented and, in due course, replaced by the 160 American cruise missiles to be stationed in this country. The United Kingdom already is, and will remain, a prime target for Soviet air attack. It is admitted that U.K. air defences against such an attack are limited. They were allowed to run down during the long period when the basis of planning was that the U.K. would be the subject of a strategic nuclear attack rather than a conventional air assault.

11. Currently the R.A.F. air defence force in the U.K. consists in the main of Phantom and Lightning interceptor fighters the effective range of which is extended to several hundred miles beyond the British coast by a force of refuelling tankers. Warning of air attack is provided by the U.K. air defence ground environment (UKADGE) comprising land-based radars and ageing airborne early warning (AEW) Shackleton aircraft. Finally, Bloodhound and Rapier surface-to-air missile squadrons are available for the defence of the base areas.

1 See evidence taken by the Defence Committee on 15th April 1980

2 Q.4

12. Against these defences the USSR can deploy a growing number of supersonic, long-range Backfire bombers, armed with air to surface (AS4) missiles with a stand-off range of up to 180 miles. There are some 80 of these bombers in the Soviet Long Range Air Force and the Naval Air Force, and their number is growing at the rate of about 30 a year. In war a high proportion could be directed against the U.K. which they could attack from the West. They could be supported, moreover, by Fencer fighter bombers from Central Europe and a large number of older Badger and Blinder bombers.

13. Plans are in hand to redress the obvious disparity between defence and attack, both qualitatively and quantitatively. In particular, the air defence variant of the Tornado will come into service in the mid-1980's. On the same time scale, the early warning arrangements are being brought up-to-date (by modernising the UKADGE and by the introduction of the Nimrod AEW aircraft to replace the Shackleton). Nine VC 10 aircraft are being converted to refuelling tankers, as a supplement to the present Victor tanker force, to give the air defence aircraft the capacity to intercept attacking aircraft well beyond their stand off missile attack range. A programme of hardening airfields has been embarked upon, albeit to be completed over a long period. These improvements will take a number of years to become fully effective. Meanwhile a new Lightning squadron is being formed, the Phantom's missile control system is being improved and some 80-90 Hawk weapons-training aircraft are being modified to carry the up-to-date AIM 9L air-to-air missile so that they could be used in an emergency.

14. The White Paper does not pretend that all this adds up to a satisfactory position. The air defence of the United Kingdom is of crucial national as well as NATO interest. If additional resources were available, the Ministry view was that the provision of additional interceptor aircraft would be the main priority but this is a lengthy and expensive business. (1) Nevertheless, until the proposed major improvements in air defence are introduced the country is not adequately defended against a major attack; the steps which are being taken to help to redress this situation both short and longer term, are to be welcomed. Among the points made in evidence to which we wish to draw the particular attention of the House are the following:

1 See for example the costs for an additional three squadrons: Q44

Paragraph 14 (Contd.)

(i) the proposed siting of 160 cruise missiles in the United Kingdom will not make much difference to the threat to the U.K. of a Soviet air attack. (1)

(ii) It is intended that 385 Tornado aircraft will be supplied to the R.A.F. They will be in two versions the strike/attack (IDS) version and the air defence variant (ADV). The first is intended for operation with NATO land and maritime forces, the second primarily for the air defence of the United Kingdom. The present intention is to allocate 220 aircraft to the strike/attack role but the distribution of the final numbers of aircraft produced between the two roles would be kept under constant review.

(iii) it would greatly increase the effectiveness of the Phantom and Lightning interceptors against the Backfire bombers if the tanker refuelling force could be augmented as planned with the greatest possible speed. In addition it would seem to be worthwhile to give further consideration to the proposal that modifications be made to the design of civil aircraft to enable them to be modified for use as tankers in an emergency. (2)

(iv) the programme for hardening airfield facilities in the United Kingdom to increase their survivability has not progressed beyond toning down structures to make potential targets less obvious from the air. Surprisingly there are currently no rapid runway repair teams yet available in the United Kingdom. This task, in which the Royal Engineers are trained for operation in RAF Germany, should be given high priority in allocation of manpower and equipment to support the United Kingdom's vital airfields. (3)

(v) the United States is responsible for the point defence of its air bases in the U.K. This could be done with suitable surface-to-air missiles. Decisions need to be taken in the United States administration and Congress within the next three months if the United States Government is to procure the British Rapier missile for this purpose within the necessary timescale. The Government have already offered RAF personnel to man Rapier squadrons at USAF bases, if the equipment is acquired. (4)

(vi) Exercise Elder Forest 80 to test the effectiveness of the U.K.'s air defences was recently completed. We hope that a full report of its results can be given during the defence debate or subsequently in the debate on the R.A.F Estimates.

1 Q58

2 Q46

3 Q64-67

4 Q26-33, 371, 373

Maritime Matters

15. We are not entirely satisfied with the assumptions on which current NATO maritime planning is founded, given the possible character of future wars. At the same time, Britain's geographical position makes it essential for her to pursue an effective maritime strategy. The Warsaw Pact's overt aim of isolating the U.S.A. from Europe gives special significance to maritime policies adopted by the Alliance. We have taken evidence on the respective strengths of the merchant fleets of countries belonging to NATO and to those who are members of the Warsaw Pact. Apart from the significance of merchant shipping in time of war, there are economic and political implications in the patterns of merchant shipping in peace. In this context we are disturbed that, while NATO countries have a larger total merchant fleet than the Warsaw Pact at present, the Soviet merchant fleet in particular is increasing in size at a time when the merchant fleets of most NATO countries are declining in numbers. The Warsaw Pact may not achieve a numerical superiority in the foreseeable future but the role of the Soviet merchant fleet is significant in terms of Soviet political and economic policies. Given the strategic significance of merchant fleets, details of their strength should be included in future White Papers.

16. The important role of submarines in anti-submarine warfare is restated in the White Paper. More nuclear-powered fleet submarines (SSNs) are being ordered and under construction and studies are well advanced for a new class of conventionally-powered patrol submarines. At present only one shipyard (Vickers at Barrow) is building nuclear-powered submarines, although another has constructed such submarines sufficiently recently for it to be able to do so again. (1) We note the serious impact on present plans to build fleet and patrol submarines which would result from a decision to build a new class of submarines to replace the Polaris boats as the British strategic nuclear deterrent. (2) We were told that if such a decision were taken, extra capital investment could be made to increase submarine-building capacity. Nevertheless, the construction of four or five nuclear-powered ballistic missile submarines would result in the loss or postponement of the production of some nuclear-powered fleet submarines. Shortage of manpower with particular skills would be an important factor in creating such a bottleneck.

1 Q. 108-112

2 Q. 116-117

17. The White Paper mentions the combined UK/Netherlands Marine amphibious force which is assigned to SACLANT for deployment in Norway, Denmark or the Atlantic Islands. We are doubtful about the UK's ability to provide the necessary amphibious lift for such a force at short notice. The Commando carriers, assault ships and landing ships, logistic, are already committed to a number of roles which would mean that they might not be readily available for transporting Royal Marines to reinforce the Northern Flank. (1) It would be unwise to rely solely on chartered ferries and serious consideration should be given to having appropriate shipping dedicated to the amphibious lift role.

18. The first of the new anti-submarine warfare carriers, HMS Invincible will be commissioned in July. We note that increased sea-based air support for the fleet (organic air) is one of the Government's priorities. (2) Organic air is very expensive. It is therefore desirable to extend the opportunities for its use in wartime without committing the Royal Navy to heavy operational costs in peacetime. The construction of more platforms on Royal Fleet Auxiliaries and merchant ships, together with the provision of more fixed-wing aircraft and helicopters (which could operate either from ashore or from ships) would provide operational flexibility without heavy running costs.

19. We were told in evidence that the United Kingdom possesses a defensive minelaying capability and that further consideration is being given to minelaying by aircraft, surface ships and submarines. The threat posed by the Soviet Fleet suggests that the Alliance should have an evident capability, not only for defensive minelaying, but also for offensive minelaying, by which hostile fleet deployments could be inhibited. We therefore welcome the belated consideration this subject is now receiving and look forward to hearing the outcome of the current review. (3) The known Soviet capability for sophisticated minelaying poses serious threats to NATO warships and merchant shipping and calls for considerable resources to be devoted to mine counter measures (MCM). We welcome the additions to the MCM force represented by the Medium Minesweepers, but heard no evidence on the use of helicopters or hovercraft except in support roles.

1 Q259, 314
2 Q278
3 Q319, 377

20. The effectiveness of the Royal Navy fleet and its support ships at sea is heavily dependent on the work of the Royal Dockyards. We note the concern about productivity in the Dockyards and about the shortage of skilled manpower both in the shipyards and in the Dockyards. (1) We await with interest the results of the current study of the role, organisation and structure of the Royal Dockyards. (2) One aspect of the Dockyards' work which has not been apparent for some years is their capacity to build new warships. This is a matter upon which there is a balance of advantage between giving the encouragement and experience of new building to a Dockyard and the depressing effect that an order forgone might have on the already under-employed yards of British Shipbuilders. In the current state of dockyard productivity, however, the argument is academic to the extent that all current commitments can only be met with extreme difficulty.

1 Q113

2 White Paper, paragraph 755

Personnel

21. The White Paper is gloomy about Services manpower. In May 1979 the total of trained personnel was well below requirement. Following the 32% increase in pay awarded to the Services by the incoming Government recruitment showed a welcome increase (though it had already begun to improve) and outflow by premature voluntary release was reduced. As a result the total strength of the regular forces increased by 4,400 between 1st April, 1979 and 1st January, 1980 compared with a steady decline in the preceding few years. The White Paper estimates, rather surprisingly, that, between 1st January, 1980 and 1st April, 1980 there will have been a fall of 2,500 in the total strength though in the subsequent year the number is expected to go up by 6,400. (1)

22. The Committee welcome the substantial improvement in pay a year ago: although it is not the only factor, pay is clearly an important element in maintaining the strength of the Services. A further increase is due from 1st April, 1980 and the Government is awaiting the report of the Armed Forces Pay Review Body. The Secretary of State for Defence told us that the Government is committed to maintaining the comparability of service pay with pay outside. (2)

23. Looking to the future, the White Paper envisages that, in the mid-1980's, the maximum requirement for trained personnel will be 20,000 greater than the present trained strength. (3) Moreover, because of the declining numbers of young men in the 16-19 age group, the Services will need to recruit 11½% of them by the end of the 1980's compared with 8½% now. Clearly, pay ought to be kept consistently at a satisfactory level in the future, but other means of dealing with what is going to be an undoubtedly difficult manpower situation need to be thoroughly explored.

1 White Paper, Volume II, page 32

2 Q389

3 White Paper, paragraph 611

24. The Women's Services total some 12,700 excluding the nursing element. This seems a very small number. An objection made to the extended employment of women is that their span of service is, on average, only half that for men. The more expensive forms of training are, therefore, uneconomic for women. The White Paper raises for public debate the possibility of women bearing arms for use in certain limited roles. The Secretary of State appears to welcome a wide debate on this matter. (1) In our view, while men in the Services may have a formal liability to carry arms, there must be very many occupations, for example in the RAF, which do not in practice call for the use of arms. Among these are air traffic control, repair and maintenance, supply, transport, catering and various headquarters and depot duties. Moreover, not all of these call for lengthy training. Short of requiring women to bear arms and without prejudice to that possibility, a more determined effort should be made to fit women into, and recruit them for, such duties.

25. Army regular and volunteer reserves comfortably outnumber the regular strength of the Army, but Royal Navy reserves are only one half of the regular strength and Royal Air Force reserves one third. The volunteer reserves of the last two Services are insignificant in numbers. In part, disparities are connected with the different mix of skills required and the different lengths of service in the three Services. Something is being done to extend the use of volunteer reserves in the Royal Navy, and the Royal Air Force. Nevertheless, it is hard to believe that there are not more roles which reservists could fill adequately in an emergency. For example, the skills required to operate many modern missiles can be learnt relatively quickly. The Secretary of State recognised in evidence the importance of reservists in the Services and wished to encourage further use of reserves. (2) We welcome his positive views on this matter. We propose that intensive efforts should be made to identify those roles and to recruit men and women for them.

1 Q400

2 Q390

26. It is essential that the reserves should be capable of being mobilised and deployed quickly in an emergency. Full mobilisation depends on certain legal steps being taken, which might have the effect of heightening tension undesirably in an already difficult situation. Even the new Individual Reinforcement Plan for regular Army and Royal Marine reservists, which the Committee very much welcomes, operates within this framework. It would seem desirable that there should be a means of calling up selected categories quickly and without contributing to an increase in tension in advance of a general mobilisation of reserves. (1) The necessary legal changes should be further studied. As to the quick deployment of reserves, we shall await with interest the publication of the results of Exercise Crusader 80, which is being held this autumn, to exercise the deployment of reserves to the Continent.

Equipment

27. Expenditure on equipment in 1980-81 is estimated at £4,752 million and will absorb about 41 per cent of the Defence Budget, the same proportion as was planned for 1979-80. £1,493 million will be spent on research and development and the remainder will be spent on production for Sea Systems £1,102 million (33 per cent), Land Systems £667 million (20 per cent), Air Systems £1,295 million (40 per cent) and General Support £194 million (7 per cent). The statistics given on p.25 of Volume II of the White Paper were based on Appropriation Accounts and Supply Estimates. As we have mentioned in paragraph 3 above, the Committee would be interested to see in future years equipment statistics based on value of contracts let. We would also welcome publication of further information about unit costs of individual systems.

28. The Committee examined some of the main elements of the planned equipment programme, bearing in mind the newer and improved equipment becoming available to the Warsaw Pact's forces. Several items of Naval equipment have been discussed under Maritime Matters in paragraphs 15 to 20 above and we here refer to some important matters of procurement for land and air forces.

29. Paragraph 709 (a) of the White Paper mentions improvements being made to the Chieftain tank and paragraph 709 (b) says that future tank requirements are receiving particular attention but there is no reference to the possible purchase of the Challenger tank for B.A.O.R. This is surprising since this project has been under consideration for a long time; the Challenger is a modified version of a tank which was being developed for the Shah of Iran; the order was cancelled by the new regime in Iran and the Royal Ordnance Factory at Leeds and Rolls Royce, the power pack manufacturer, were forced to reduce their workforces. The question of whether or not to provide the Army with the Challenger has therefore important employment as well as other implications. The Committee were told by the Secretary of State that a decision on purchase could not be made until all the implications had been thoroughly considered. (1) Matters to be weighed were operational requirements; suitability for use in Europe; manpower, logistic and budget effects and influence of a purchase on provision of a new tank for the 1990's. A decision is unlikely to be announced before the autumn. (2)

1 Q416-132
2 Q154, 155

30. Decisions are however expected to be taken very shortly on some important new systems, for example the mechanised combat vehicle (MCV), the improved Harrier and the tracked Rapier. Development in the United Kingdom of a vehicle (MCV 80) to replace the infantry armoured personnel carrier fleet has been proceeding for some time; about 2,000 vehicles will be required by the mid-1980's. The United States is also developing an infantry fighting vehicle (IFV) and progress on this is being monitored as a possible alternative to MCV 80. Both vehicles will meet the Army's requirement in broad terms. The Ministry are examining their target in-service date and the cost and production implications of selecting the U.S. vehicle. A decision is expected by July 1980. The level of armament of the MCV still has to be considered. It is planned currently to have Rarden guns which would be effective against Soviet tanks but only at short range and depending on where a hit was made. The IFV would have a small calibre gun with a markedly higher rate of fire. (1) In our view the level of armament to be fitted is of crucial importance and we may wish to revert to this matter.

31. Paragraph 715 (d) of the White Paper says that consideration is being given to whether the U.S. Marine AV8B or the improved Harrier being designed by British Aerospace, could meet the requirement for an improved Harrier. It is not yet certain that the U.S. Government will approve the AV8B programme. We were told that the British Aerospace version could well be a cheaper option than participating in joint production arrangements for the AV8B to meet the R.A.F. requirement. (2) The Ministry expect to make their decision by early summer. (3)

32. Paragraph 712 states that a tracked version of the Rapier Low Level Air Defence weapon is being evaluated. This could be in service by the mid-1980's if development proceeds smoothly. Evaluation is likely to be completed in time for a decision to be taken before the end of the year. (4)

33. The Committee raised in evidence the progress of the Tornado programme and whether the numbers of each version planned to be ordered had been reviewed, 146 of the G.R.1. version have so far been ordered for the R.A.F. out of a total planned order of 220. The Air Defence F.2 version, which is being developed specially for the R.A.F., flew for the first time in October 1979 and aircraft will not enter service until the mid-1980's. The Secretary of State told us that he was not proposing to make any alterations to the balance of the orders for the two versions in the immediate future. However, the programme was flexible and the Government could decide to purchase a different mix of versions within the same total order. The matter would be kept under review. (5)

1 Q162-3
3 Q213
5 Q374

2 Q200, 203, 206
4 Q187, 191

34. The United Kingdom Air Defence Ground Environment (UKADGE) is a network of operations centres, communications systems and surveillance radars. It acts as the command and control system for the United Kingdom air defence forces and its facilities are being improved in a programme expected to be completed in the mid-1980's. Much of the programme is being financed from NATO infrastructure funds, including seven of the twelve radars and the Command and Control System, and these parts will therefore be subject to international competition. Two consortia are bidding for the provision of the Command and Control facility but the Ministry will have no idea of the likely balance between the American, British and European contents of the equipment until bids are received in May 1980. The Ministry told us that the successful contractor for the first seven NATO-financed radars would not necessarily win the competition for the other five nationally-financed ones although they would be in a good position to do so. (1) The Committee would expect British systems or British components to be adopted to the maximum possible extent consistent with getting value for money.

The Industrial Base

35. The development and production of equipment to meet the needs of the Services are shared between the Ministry of Defence's own research and development establishments, the Royal Ordnance Factories and industry. The White Paper states that over 20 per cent of the output of the electronics industry and over 60 per cent of work in the aerospace industry is for defence purposes and the defence equipment programme sustains directly or indirectly about 400,000. (2) The Secretary of State told us that he is in no doubt about the importance of this home-based arms industry. (3)

36. Some 75 per cent of the equipment budget is spent on national contracts placed with British industry and between 15 and 20 per cent as the United Kingdom share of collaborative projects. (4) The Ministry, however, do not pursue a stated policy of buying British. Each case is looked at individually with regard to performance, time-scale and cost, and the probable effect on employment and on maintaining a design capability is taken into account. In coming to a decision the Ministry are biased in favour of buying nationally even if this results in some penalties in time or cost in particular cases. (5)

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- 1 Q50-56
 - 2 Paragraphs 734, 735
 - 3 Q406
 - 4 Q406
 - 5 Q407

37. Defence Sales cover a wide range of systems and associated services including air defence, communications and radar systems and technical assistance. In 1980-81 these sales are expected to amount to some £1,200 million and to provide some 75,000 direct jobs in British industry. Customers are mainly non-NATO countries because well developed arms industries in Western Europe make market penetration there difficult and the United States unfortunately has so far been reluctant to adopt European equipment. Transatlantic sales are about four to one in favour of the United States and the two way street has not developed as we would have hoped. (1) We welcome the statement in paragraph 749 of the White Paper noting the constraints on the pursuit of arms sales.

38. The Committee is pleased to note the scale of support for British industry and would endorse the Ministry's practice of buying nationally to the greatest possible extent consistent with defence needs, and of seeking collaboration with allies in appropriate cases. We consider that the series of forthcoming decisions on the purchase of major items such as the Mechanised Combat Vehicle, the Ground Environment radars, and the Harrier improvement should be viewed in the context of the industrial base required to support major defence commitments. To get the value for the money allocated for Defence it is the responsibility of the Ministry to obtain the best equipment at the right time and at the most economical price. Nonetheless the Government as a whole cannot ignore the additional benefit which home produced equipments have on employment, exports, and the technological base. There is no evidence that other NATO Governments are prepared to ignore their own domestic interests. It would not be sensible for the British Government to do so.

The Defence Budget

39. The White Paper shows that defence spending for 1980-81 is planned to be 3½% higher in real terms than the estimated outturn for 1979-80. But actual spending on defence last year is expected to show a volume shortfall of some £200 million or 2.3% on original plans. (1) Thus the difference between spending plans for 1980-81 and those for 1979-80 is an increase of only about 1%. There has been a tendency in recent years for actual defence spending each year to fall below the level planned for that year. In 1978-79 the volume shortfall was £182 millions or 1.5% of the defence budget. If underspending in 1980-81 is more than ½% of the planned expenditure, Britain will fail to achieve the 3% increase agreed with her NATO partners. In this context we consider that the Ministry of Defence should be empowered to carry over underspending from year to year.

40. Although the proportions of the defence budget devoted to equipment and to forces' pay are almost exactly the same as last year (41% and 17% respectively) the combination of better pay for the Armed Forces and increased recruitment will lead inevitably to pressure on other parts of the budget. At the same time, the ending of the offset agreement with West Germany over the costs of BAOR will place an added strain on the defence budget. Even within the planned real increases in defence spending, there will be considerable difficulty in finding room for the expensive programmes which lie ahead - Jaguar/Harrier replacement, the main battle tank, the Sea King replacement, MCV, ASW cruisers, UKADGE and so on. This is quite apart from any costs which may arise when the Polaris nuclear deterrent force is replaced. In evidence the Secretary of State told us that, given that the expenditure would fall at different times, he hoped to be able to fit it all in, though higher annual increases might be needed to meet these commitments. (2) The scale of increases in the real costs of each new generation of weapons system which has been illustrated by Ministry of Defence analysts (3) makes it seriously open to doubt whether there will be room for all these projects in the defence budget in the desired timescale. It may be that whereas weapon systems will need to be replaced rapidly with advances in technology in future years, delivery platforms such as ships and aircraft will have to be designed to be able to be fitted with successive generations of weapons over a longer period.

1 Cmnd. 7841 page 23

2 Q420

3 Q421

41. The White Paper provides a valuable illustration of the extent to which future spending on major equipment is already committed by decisions made in the past. In the year immediately ahead, 90% of expenditure is tied up in advance and decisions taken now will only be able to affect 40% of the procurement budget in seven years' time. This shows both the immense importance of long term planning and costings and the limitations imposed on decision-making for the short-term. We believe that there is a case for planning for a longer period ahead than is included in the long-term costings. Not only is it important to plan individual projects well in advance but also it is essential to assess how they fit with other projects into the defence budget for future years. The consequence of not doing so is the risk of cancelled projects and wasted resources.

42. Planning defence spending over a decade or more involves critical decisions about the allocation of resources between particular activities. We are not satisfied that the Ministry has addressed itself to the question of resource allocation in sufficient depth. This is a subject which we consider to be of considerable importance and we may wish to return to it in the future.

Conclusion

43. We have met on seven occasions within a nine day period on this inquiry which has placed a great strain on all those connected with producing our Report and evidence. We regret that the time-table imposed upon us by the short time between publication of the White Paper and the debate has limited the scope of our inquiry. We intend to give future White Papers closer scrutiny.

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PROCEEDINGS OF THE DEFENCE COMMITTEE

Tuesday 15th April 1980

Members present:

Sir John Langford-Holt (in the Chair)

Mr. John Cartwright	Sir Timothy Kitson
Mr. Bernard Conlan	Mr. Allen McKay
Mr. Bruce George	Mr. Michael Mates
Rt. Hon. Dr. John Gilbert	Mr. Cranley Onslow

The Committee deliberated.

Ordered, That, unless otherwise ordered, strangers be admitted during the examination of witnesses this day, tomorrow and on Thursday 17th April.

Mr. J. Peters, Assistant Under Secretary of State (Air Staff), Air Vice-Marshal P. B. Hine, FBIM, Assistant Chief of the Air Staff (Policy), Air Commodore R. Colbeck, Director of the Air Defence Environment Team (RAF), Ministry of Defence, called in and examined.

[Adjourned till tomorrow at
half-past Ten o'clock

Wednesday 16th April 1980

Members present:

Sir John Langford-Holt in the Chair

Mr. John Cartwright	Sir Timothy Kitson
Mr. Bernard Conlan	Mr. Allen McKay
Mr. Bruce George	Mr. Michael Mates
Rt. Hon. Dr. John Gilbert	Mr. Cranley Onslow

The Committee deliberated.

Draft Appendix to the Committee's First Report (Ammunition Storage Sites for British Forces Germany), proposed by the Chairman, brought up, read and agreed to.

Ordered, That the Appendix be added to the Report.

Ordered, That the Chairman do make the Report to the House.

Ordered, That the provisions of Standing Order No. 85 (Select Committees (reports)) be applied to the Report.

Mr. K.C. MacDonald, Assistant Under Secretary of State (International and Industrial Policy), Mr. M.G. Power, Assistant Under Secretary of State (Naval Staff), Mr. A.W. Stephens, Assistant Under Secretary of State (General Staff), Mr. J. Peters, Assistant Under Secretary of State (Air Staff), Mr. W. Meakin, Managing Director, Royal Ordnance Factories, and Mr. L.J. Rydill, Director of Ship Design and Engineering, Ministry of Defence, called in and examined.

[Adjourned till this day
at half-past Four o'clock

Wednesday 16th April 1980

ii

Members present:

Sir John Langford-Holt in the Chair

Mr. John Cartwright	Rt. Hon. Dr. John Gilbert
Mr. Bernard Conlan	Mr. Allen McKay
Mr. Bruce George	Mr. Cranley Onslow

The Committee deliberated.

Mr. M.G. Power, Assistant Under Secretary of State (Naval Staff), Rear Admiral S.A.C. Cassels, CBE, Assistant Chief of the Naval Staff (Operational Requirements), Captain J.F. Woodward, RN, Director of Naval Plans, and Group Captain J.F. Willis, Deputy Director of Air Plans (RAF), Ministry of Defence, called in and examined.

The witnesses withdrew.

The Committee further deliberated.

[Adjourned till tomorrow at
a quarter to Four o'clock

Thursday 17th April 1980

Members present:

Sir John Langford-Holt in the Chair

Sir Frederic Bennett	Sir Timothy Kitson
Mr. John Cartwright	Mr. Allen McKay
Mr. Bernard Conlan	Mr. Michael Mates
Mr. Bruce George	Mr. Cranley Onslow
Rt. Hon. Dr. John Gilbert	

The Committee deliberated.

The Rt. Hon. Francis Pym, M.C., a Member of the House, Secretary of State for Defence, was examined.

[Adjourned till Monday next
at half-past Four o'clock

Monday 21st April 1980

Members present:

Sir John Langford-Holt in the Chair

Mr. John Cartwright	Mr. Allen McKay
Mr. Bruce George	Mr. Michael Mates
Rt. Hon. Dr. John Gilbert	Mr. Cranley Onslow

The Committee deliberated.

Resolved, That an italicized rubric be included on the Order Paper under the main motion for the defence debate referring to the Committee's forthcoming report on the Statement on the Defence Estimates.

[Adjourned till Wednesday next
at half-past Ten o'clock

Wednesday 23rd April 1980

Members present:

Sir John Langford-Holt in the Chair

Mr. John Cartwright	Sir Timothy Kitson
Mr. Bernard Conlan	Mr. Allen McKay
Mr. Bruce George	Mr. Michael Mates
Rt. Hon. Dr. John Gilbert	Mr. Cranley Onslow

The Committee deliberated.

Draft Report (Statement on the Defence Estimates 1980), proposed by the Chairman, brought up and read.

Ordered, That the proposed Report be read a second time, paragraph by paragraph.

Paragraph 1 to 3 read, amended and agreed to.
Paragraph 4 read, as follows:

4. Given the Government's apparent commitment to providing information, we regret that it was found necessary to make the cost of the two volumes of the White Paper £8.50p. While this is for two volumes it nonetheless compares unfavourably with the cover price of £2 on the White Paper for 1979. Other countries such as the Federal Republic of Germany and the United States make little or no charge. We welcome the new presentation and increased amount of material published but, in our conviction that defence information should be as widely disseminated as possible, we recommend that the Government should review their pricing policy for this important publication.

Paragraph disagreed to.

Paragraphs 5 to 8 read, amended and agreed to.
Paragraph 9 read, as follows:

9. One aspect of the British position which is of great concern is the foreign exchange cost of the British Forces in Germany. The previous administration, in making the last offset agreement signed in 1977, allowed for the ending of offset payments by the Federal Government at the end of the last financial year. The position whereby the British forces are contributing to the defence of the Alliance, but at the same time are adding to the strains on the British economy, cannot be of long term benefit to the Alliance.

Paragraph disagreed to.

Paragraph 10 read, as follows:

10. We put to the Secretary of State questions concerning the place of France within NATO. We note the assurance which he felt able to give about the fundamental commitment of France to the Alliance. It would, of course, be more efficient and cost effective if France were a fully integrated member of the military structure of the Alliance.

Paragraph disagreed to.

Paragraphs 11 to 23 read, amended and agreed to.

Paragraphs 24 and 25 read and agreed to.

Paragraphs 26 to 29 read, amended and agreed to.

Further Consideration of Report adjourned till later this day.

[Adjourned till this day at
Five o'clock

v

Wednesday 23 April 1980

Members present:

Sir John Langford-Holt in the Chair

Mr. John Cartwright
Mr. Bernard Conlan
Mr. Bruce George

Rt. Hon. Dr. John Gilbert
Sir Timothy Kitson
Mr. Allen McKay

The Committee deliberated.

Consideration of Draft Report (Statement on the Defence Estimates 1980) resumed.

Paragraphs 30 and 31 read and agreed to.
Paragraphs 32 to 34 read, amended and agreed to.
Paragraph 35 read and agreed to.
Paragraphs 36 to 38 read, amended and agreed to.
Paragraph 39 read, as follows:

39. The Secretary of State told us that he is in no doubt about the importance of this home-based arms industry. It ensures supply; it enables British Service requirements to be met in an appropriate and timely way and paid for in sterling; it is helpful in developing new technology; it enables the U.K. to collaborate where this course is preferable and it offers the prospect of securing foreign exchange through sales.

Paragraph disagreed to.

Paragraphs 40 to 46 read, amended and agreed to.

A Paragraph brought up, read the first and second time, and inserted.

Resolved, That the Report, as amended, be the Second Report of the Committee to the House.

Ordered, That the Chairman do make the Report to the House.

[Adjourned till Wednesday next
at half-past Ten o'clock



From the Secretary of State

CONFIDENTIAL

The Rt Hon Francis Pym MC MP
Secretary of State for Defence
Ministry of Defence
Main Building
Whitehall
London, SW1A 2HB

30 May 1980

Dear Francis

MILITARY TRAINING ASSISTANCE FUNDS

I have seen the recent minutes on this subject, which correctly suggest that I would have an interest in the implications of any contingency scheme to enable the United Kingdom in an emergency to provide military equipment on subsidised terms.

My Department is of course already involved in the Review of Defence Sales Policy which was set in train by an exchange of minutes between yourself and the Prime Minister's Private Secretary in January, and the point came up briefly at the meeting of Ministers and officials which Cecil Parkinson attended on 27 February to launch that Review. It might therefore be most convenient to give this question the careful examination it deserves as part of the review of our support for defence sales generally.

I am copying this letter to the Prime Minister, the Foreign and Commonwealth Secretary, the Chancellor of the Exchequer and Sir Robert Armstrong.

*Yours ever
John*

CONFIDENTIAL

JOHN NOTT

1967
MAY 30

30 MAY 1967

CONFIDENTIAL



Defence

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

22 May 1980

The Rt Hon Lord Carrington
Foreign and Commonwealth Secretary

NBPA

John Pate

Phms

UK MILITARY TRAINING ASSISTANCE (UKMTAS)

Thank you for your minute of 16 May.

I agree that your ideas for a contingency scheme for supply of military equipment should be looked into by officials of the departments concerned. But I suggest this can best be accomplished through the usual Whitehall channels on the basis of specific proposals by your Department. The UKMTAS study will call for a great deal of work, and I really think the new MISC 42 Committee should concentrate on that alone.

I am, of course, willing to look at the costed assessment of Zimbabwe's military assistance needs, when General Fursdon's report is to hand. But I cannot accept, in advance of detailed consideration of the issues, that any part of the cost must necessarily be found from the central contingency reserve.

I am copying this to the Prime Minister, Francis Pym, John Nott and Robert Armstrong.

2 -

GEOFFREY HOWE

John

27 MAY 1980

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CONFIDENTIAL

FCS/80/92

CHANCELLOR OF THE EXCHEQUER

Prime Minister
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(2)

United Kingdom Military Training Assistance (UKMTAS)

1. Thank you for your letter of 8 May.

2. I am glad you agree that a review of our military assistance policy should be put in hand. I am sure your suggestion that it would be helpful for your officials to be involved in it from the outset is right. As for the "contingency scheme for supply of military equipment", I think we should allow officials to look into this. The financing of anything which may emerge will clearly be an important factor in determining whether we should get into that area or not. But there are issues of principle involved as well. I should like to see the case for and against properly argued. I hope this will not present you with a great difficulty. I agree that there may be advantage in John Nott's people being involved in that aspect of the review. No doubt Robert Armstrong will bear their interest in mind.

3. You also mentioned the problem you foresaw over providing additional military assistance funds to cover the needs of Zimbabwe. I quite accept the need to keep public expenditure under control. However, your letter to me of 28 March suggested that you would look at this again when we had a costed assessment of what may be required. I expect to have that assessment shortly.

4. The most serious threat to the Zimbabwe settlement, in which we have invested so much, comes from the security situation and the problems involved with the integration of the three armies. Mr Mugabe stressed this when he saw the Prime Minister last week and he made a special plea for more British instructors to train the new Zimbabwe Army. The Prime Minister said that we should follow up this request, and Mr Mugabe will be expecting

/us to try

CONFIDENTIAL



us to try to meet his requirements as a matter of urgency. The funds now available will cover our present military training team of 58 for six months (at a cost of some £0.75 million) and some items of training in the UK. General Fursdon is discussing with Mugabe the details of his further requirements and I cannot pre-judge what will be recommended. But it seems likely that we shall need at a minimum to provide for a larger training team for a full year. Zimbabwe's needs will, as far as possible, be met from our £7.2 million worldwide Military Assistance Vote. One seventh of this (£1 million) is earmarked for Zimbabwe. That £1 million will not, however, be enough. For the reasons I have set out before, I cannot justify reducing further the military assistance allocations to other important areas such as the Middle East, the Caribbean and South East Asia.

5. I hope that you will agree to look again at this particular requirement when General Fursdon's report is to hand.

6. I am sending a copy of this minute to the Prime Minister, Francis Pym, John Nott and Robert Armstrong.

[Approved in draft by Lord Carrington]

RM/Lyne

pp. (CARRINGTON)

Foreign and Commonwealth Office

16 May 1980

16 MAY 1980

16 MAY 1980

CONFIDENTIAL



DEFENCE

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

The Rt Hon Lord Carrington
Secretary of State for Foreign
and Commonwealth Affairs

8 May 1980

Law Puk

*WBRN yet
Puk - 9/6*

MILITARY TRAINING ASSISTANCE FUNDS (MTAF)

I have read with interest your minute of 25 April to Francis Pym. I see the case for a review of policy on MTAF, and I think it would be helpful if Treasury officials took part as appropriate. One issue which would I hope be explored is the cost-effectiveness of MTAF as a means of promoting increased defence sales. It could be that more direct marketing methods are more cost-effective.

I note that you envisage that officials would also consider 'the implications of a contingency scheme to enable the UK in an emergency to provide military equipment on subsidised terms'. It is not clear to me just what would be involved in such a scheme, and how you envisage that the subsidies would be financed. John Nott's interest is obvious, and perhaps his and ECGD officials ought also to be brought in. I suspect that this is really a separate issue from that of military training.

I was grateful for your warning that you had found it impossible to divert to military training assistance further financial resources from the civil aid programme, and that you might need to approach me again for additional funds, specifically for Zimbabwe, when you have General Fursdon's report. I fear that I can only give a similar warning that, since it was only in mid-March that we decided upon the four-year, £75 million, aid programme for Zimbabwe (which involved a call on the Central Contingency Reserve this year and next), I would not be prepared to contemplate reopening that issue now. It really is essential that we keep the lid on public expenditure.

/I am copying

CONFIDENTIAL



I am copying this letter to the Prime Minister, the Secretaries of State for Defence and for Trade, and to Sir Robert Armstrong.

GEOFFREY HOWE

Handwritten signature and initials

4-8 MAY 1980

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CONFIDENTIAL



NB DOT MAP

7/1.
Defence

MINISTRY OF DEFENCE WHITEHALL LONDON SW1A 2HB

TELEPHONE 01-218 9000 2111/3
DIRECT DIALING 01-218

MO 24/4

6th May 1980

Dear Peter,

Thank you for your minute of 25th April, in response to mine of 10th March.

Given the difficulty and reluctance with which I agreed that MOD votes could contribute exceptionally for 1980/81 to the UKMTAS programme, I am naturally disappointed that you have not, in the event, found it possible to make even a modest additional contribution from within the FCO's budget. I share your concern that we should plan ahead on the basis of a consistent and comprehensive policy for the allocation of UKMTAS funds, and endorse your proposals for an official review the terms of which are, I think, sufficiently general to meet the requirement. It is appropriate that the remit should refer specifically to the UK funded part of the programme, but a substantial proportion of the Commonwealth and foreign training provided by the MOD is, of course, paid for by the recipient Governments. I am sure you would agree that this should be given due weight in the review.

Our officials will now need to make an early start, in order to meet the PESC deadline. A good deal of work both within and between our Departments is called for, if we are fully to meet the concerns I outlined in my minute of 10th March. It is clearly important, however, that decisions on the financial resources which military assistance requires should not be held up to take account of any further studies which may be required.

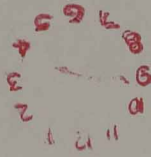
I am sending a copy of this minute to the Prime Minister, the Chancellor of the Exchequer and to Sir Robert Armstrong.

James Lee

Francis Pym

Francis Pym

The Rt Hon The Lord Carrington KCMG MC
CONFIDENTIAL



1-7 MAY 1980



FCS/80/80

SECRETARY OF STATE FOR DEFENCEMilitary Training Assistance Funds

1. I am most grateful for the offer of a £2 million transfer from your cash limits to mine which you made in your minute of 10 March, knowing how difficult that decision was for you in the light of your own problems.
2. I am sorry not to have replied sooner to your minute. But, as you suggested, I have been looking very carefully again at the Civil Aid programmes as a source of the remaining shortfall in the military assistance budget. Alas, it is clear that, try as I might, it simply is not possible to shave a further £1 million off the already much reduced civil aid provision.
3. The military assistance programme will be squeezed even more by the need to help Zimbabwe, despite your contribution of £2 million. Indeed I have already allocated half that sum to Zimbabwe; but even this is not nearly enough. I shall need to approach Geoffrey Howe again when we have the detailed report on Zimbabwe's needs from General Fursdon.
4. The difficulties we have had this year over funding underline the point you make about the need for a review of our overall policy on military assistance. In fact this is the second year running when we have only been able to mount an effective programme at the last moment and in a very ad hoc manner. I know that you share my view that our military training assistance programme is perhaps the most cost effective of all the measures we can take to help the security of third world countries. We must face up to the implications of this and so arrange things that we can plan ahead on the basis of a consistent and comprehensive policy.
5. Before we begin consideration of PESC for 1981/82 onwards, I would like to put to colleagues realistic proposals for the future scale, funding and organisation of our military assistance. With this in view I am sure it is right that your officials and mine (and, if Geoffrey Howe agrees, Treasury officials also), should meet

/soon



soon under Cabinet Office Chairmanship to review this whole area of policy. They will need to work quickly so that I can report to colleagues by the end of June. I propose that their remit should be to examine and make recommendations on:

- (a) the scale, nature and financing of the UK funded military assistance programme covering both the training of overseas students in the UK and the provision of training advice by British Loan Service Personnel;
- (b) the implications of a contingency scheme to enable the UK in an emergency to provide military equipment on subsidised terms.

6. I am sending a copy of this minute to the Prime Minister, the Chancellor of the Exchequer and to Sir Robert Armstrong.

C

(CARRINGTON)

FOREIGN AND COMMONWEALTH OFFICE

25 April 1980

25 APR 1980



CONFIDENTIAL

Defence 2
~~PRIME~~
PDC (80) 2 / MINISTER
MS

STATEMENT ON THE DEFENCE ESTIMATES 1980

CMND. 7826

It is hoped that Members will find the attached notes useful during the two-day Debate on this White Paper on Monday, 28th April/Tuesday 29th April 1980.

Conservative Research Department,
32, Smith Square,
London, S.W.1.

mt

CPAJ/FJVB
24th April, 1980

STATEMENT ON THE DEFENCE ESTIMATES 1980

CMJ. 7826

"DEFENCE IN THE 1980s"

I N T R O D U C T I O N

1. A basis for informed Public Debate

Addressing the Annual Conference of the Greater London Young Conservatives in Birmingham on 12th April, 1980, Mr. Francis Pym, Secretary of State for Defence, said:

"Just before Easter, the Government published its first Defence White Paper. In it we sought to present fully and clearly the facts and major defence issues as we see them as a basis for the informed public debate about defence which we believe necessary to the success of our defence policy:

- * This White Paper sets out more clearly than ever before the threats which Britain and our allies must expect to face in the 1980s.
- * It sets out the Government's response - and the belief we have in our continued commitment to the North Atlantic Alliance.
- * It sets out our acceptance of increases in defence spending at a time when restoration of our economic health demands cuts in public expenditure overall.
- * It describes our contribution to NATO's nuclear and conventional forces.
- * It explains that we are considering certain improvements to the Services' capability to operate flexibly outside the NATO area.
- * It stresses our continuing commitment to give proper treatment to the Services, in terms both of pay and conditions of service; to improve recruitment and retention; and also to improve the women's services, and it raises the question of the arming of women. Our prompt action on pay has already helped towards a better level of morale and recruitment... Defence spending is not an alternative to spending on other public programmes so much as a pre-condition for them; it allows us to assure our basic security without which the free and peaceful pursuit of our national life would become impossible. The scale of our general economic capability, and the wider constraints on resources put us on our mettle to achieve the utmost economy in allocating the means at our disposal. Our ability to spend even more on defence depends ultimately on the basic prosperity of our nation.

As a Government we are steadfastly pursuing the only economic policies that will in the end remedy our economic problems, and in that remedy lies the secret of yet greater defence strength".

2. A new format

This White Paper is new in format and ambitious in scope. It is divided into two volumes:

Volume I discusses in a full and open way the underlying principles of our defence effort, the issues and problems facing the Government, and the decisions which have set the guide lines for defence spending not only in 1980 but for several years to come.

Volume II contains a comprehensive collection of defence statistics.

3. Some press reactions

- a. This White Paper "steps firmly in the right direction by disclosing more facts, and considerably more figures, than has previously been the case. The Government's objective is to make people more aware of the issues before the country, and to ensure that the debate which might ensue is informed and constructive". (Times, 3rd April, 1980).
- b. "... the first White Paper on defence to be published by the Conservative Governemnt is significant in two ways. On the one hand, it fulfils the Manifesto commitment to increase defence spending in real terms, a commitment that has become more urgent since the Soviet invasion of Afghanistan. On the other hand, it gives a much fuller account of official defence thinking than we have recently been accustomed to. It discusses the problems as well as the policies and the aspirations". (Financial Times, 3rd April, 1980).
- c. "... It also reviews the global defence scene in a far more detailed manner than in previous years". (Daily Telegraph, 3rd April, 1980).

B A C K G R O U N D

4. Labour's Legacy

The Labour Governemnt cut £12,000 million off planned defence expenditure up to 1983-84 and, according to their Election Manifesto Labour aimed to reduce defence spending even further. As a result, our defences were reduced below the safety level and the Services' confidence was shaken to a point where the loss of trained manpower was reaching alarming proportions. Further details of the effects of Labour's cuts are at Annex A.

THE WHITE PAPER - VOLUME I

(Numbers in brackets refer to paragraphs of the White Paper unless otherwise described).

5. Introduction (pages 1 & 2)

The Introduction stresses the importance that the Government attaches to defence. The fate of Afghanistan is a reminder that continued peace, security and freedom cannot be taken for granted or enjoyed free of charge. Although the scale of our defence effort cannot be considered in isolation from the UK's general economic condition, the Government's aim is to restore our defences to the level needed to provide the best guarantee of security, using the most economical means available and in full consciousness of the complex judgements this requires.

It states:

"Without the national security which defence capability provides, plans to contain inflation, restore incentives, secure economic growth, improve our health care and our children's education rest on sand". (page 2).

6. The context of Britain's Defence Policy (Chapter 1).

a. The Warsaw Pact Threat

Portions of both Chapters 1 & 2 (see Index) outline many important and familiar aspects of this threat concluding that "the Soviet forces facing NATO are very much larger than would, in our judgement, be needed for defence alone". (109). This reflects two statements made by the Prime Minister in recent speeches:

(i) "By extending her own armament efforts, the Soviet Union compels others to do likewise... They choose to arm themselves for offence. We look only to our defence." (Guildhall, 12th November, 1979).

(ii) "The Russians do not publish their intentions. So we must judge them by their military capabilities, ... The restoration of a military balance is not an end itself. It is a necessary condition for the development of relations between the East and West". (Luxembourg 12th October, 1979).

b. The following extracts from a recent "backgrounder" issued by the U.S. International Communication Agency on 3rd April 1980, supplements the information contained in the White Paper:

(i) Since 1968, the number of Soviet divisions deployed in Eastern Europe has increased from 26 (roughly 250,000 men) to 31 (about 370,000 men) - larger in size and with vastly increased fire-power.

..... / (ii) The Soviet Union

- (ii) The Soviet Union has three times as many Theatre Nuclear Weapons with ten times the throw-weight as NATO has in Europe.
 - (iii) The Soviet Union is turning out modern tanks at the rate of 3,000 each year.
 - (iv) The Warsaw Pact has twice as many operational airfields as NATO - roughly 400 against 200.
 - (v) Among the Warsaw Pact advantages cited by military analysts are: standardization of equipment, a highly flexible logistics system, a preponderance of offensively - oriented armour, better air defences and more usable airfields, closed societies - which lend themselves to secrecy - and basic geography.
- c. For the third year running the International Institute for Strategic Studies has warned that the military balance between NATO and the Warsaw Pact is "moving steadily against the West". ("The Military Balance 1979-80").

b. NATO and the EEC

In the context of the sections on The North Atlantic Alliance (112-119) and Alliance Strategy (120-129) it is perhaps appropriate to draw attention to our attitude to the relationship between NATO and the EEC:

- (i) In a major speech on foreign affairs in Brussels on 23rd June 1978, Mrs. Thatcher called, amongst other things, for an end to "confusion of purpose in the West", arguing for a closer relationship between NATO and the EEC - "two great organisations both concerned with the protection and prosperity of Western Europe but which have little to say to one another".
 - (ii) Addressing a CDU security policy forum at Kiel on the 13th January 1978, Sir Ian Gilmour, then Shadow Defence Secretary, said:

"As to the European aspect of the collective defence effort: First of all it should not be purely European. We should lift our eyes occasionally from the central front and from the flanks and remember that the threat is world wide and not confined to Europe. And of course it should not be purely European in another sense. While I am strongly in favour of as much European co-operation in defence as possible, there can be no question of a purely European defence policy. Our alliance is an Atlantic one and anything that tends to separate the United States and Canada from their European allies should be avoided."
- c. In a speech in London on 19th December 1978, Mr. Francis Pym, Shadow Foreign Secretary, said, "... our future prosperity and, more significant still, our future security, depend upon the complementary alliances of the EEC and NATO, the one economic, the other protective".

- d. On 26th January 1979 at Cambridge, Mr. Pym said, "Without the economic security and stability that membership of the Community provides, Britain cannot make her full and proper contribution to her partnership with other states in Europe and the USA in NATO, which alone can provide the military security on which her political freedom and stability depend".

7. The British Contribution to NATO's Nuclear Forces (Chapter 2)

The role of nuclear weapons in Britain's defence policy was debated on 24th January 1980 (Hansard Columns 672-784). Copies of the CRD brief for this debate (PDC (80) 1) are available in the Whips' office.

8. Wider Defence Interests (Chapter 4)

a. Towards a more global approach

Addressing the Royal College of Defence Studies on 5th December 1979 Mr. Pym said:

- "The security policy of a country with the interests and history of the United Kingdom cannot be confined to the NATO area especially since Soviet ability and inclination to act against Western interests world-wide is growing. We have to be and want to be outward looking, and within the very heavy constraints imposed upon us, largely arising from the uncertainties in the British economy, we are determined to do this to maximum possible extent".
- "... the willingness of the Soviet Union and its Warsaw Pact and Cuban allies to interfere in the countries of the Third World represents a threat to stability which may have serious consequences for the West if it is allowed to go unchecked".
- "A major indicator of the Russians' growing interest on the global projection has been the remarkable development over the last 20 years of the Soviet Navy. Between 1968-1978 the number of Soviet naval ports visits trebled. From being a small coastal navy, Admiral Gorschkov has created a mighty tool of Russian foreign and defence policy. This development continues - every 45 days a new Russian submarine is launched. The powerful Soviet fleet could be used anywhere in the world to disrupt shipping lanes on which the Western trading nations including the United Kingdom rely".
- "... We must signal to the Soviet Union and its allies a willingness to protect essential interests by military means, should the need arise. The task cannot be shouldered by the United States alone - despite their quite massive contribution of muscle and their tremendous strength of will. It must be shared by every country of the United Kingdom's European partners".
- "Given the growing threat to Western interests and the

..... / range of our commitments,

range of our commitments, it is important that the United Kingdom should have an adequate military capability to operate outside the NATO area, where the need arises, without eroding our essential military commitment to the Alliance. Some improvements in the Services' world-wide capability may therefore be needed.

He went on to outline the proposals then being considered. These are now reflected in paragraph 409 of the White Paper.

- b. In paragraph 402, referring to our "wider interests" the White Paper states:

"In common with our NATO allies, we also have wider interests outside of the NATO area which we cannot afford to neglect. We depend on the developing world for many raw materials. The security of our trade routes is therefore of vital importance to our economy and we have a substantial practical interest in the stability of the countries with whom we trade".

In this connection, in a speech in London on 8th March, 1979, Mr. Pym, then Shadow Foreign Secretary, referring to Russia's expansionist activities said:

"... Russia has extended her subversive activities over a wide area - to Ethiopia, Afghanistan, South Yemen and Zaire. At the same time Russia has extended her mercantile activities all over the world. She has built up a global fleet which poses a major threat to our supplies of vital raw materials - especially in Southern Africa - and to our trade routes everywhere".

During a debate on 25th May 1979, on South Africa (Trade) Mr. Cecil Parkinson, Minister of State, Department of Trade, said:

"Our imports from South Africa are mainly raw materials, which are of great importance for our economy. I understand what my Hon. Friend said, that it is not only this country which depends on South African chromium, manganese, platinum and vanadium. He pointed out the strategic consequences of this dependence and outlined who controls the alternative sources of supply. It cannot be overstressed that these vital minerals are important to the West, not just to its interest as a trading bloc but to its defence. There is a similar dependency throughout the whole industrialized world". (Hansard Col. 1388).

9. Personnel

a. Pay (607-8)

The AFPE is expected to send its report and recommendations on this year's pay award to the Prime Minister at any time.

b. The reserves (616-20) and the Cadet Forces (622)

In a speech at Ponteland on 19th April Mr. Pym said:

- "Without the vital contribution of the TA and other

..... / reservists we could not

reservists we could not provide the additional military strength necessary to meet our defence commitments".

- "The importance of the Cadets and Reserves is not simply that they provide a framework within which defence and the community can be integrated at all levels, but also that they provide a way in which people can make a direct personal contribution to the defence of our country - a contribution in which those who believe in freedom and the democratic way of life and the independence of our nation, can stand up and be counted".

10. Defence Sales (749-50)

The Secretary of State visited China from 23rd-26th March. In a Written Answer on 31st March concerning the sale of military equipment to China, Mr. Pym described his discussions with the Chinese Defence Minister on the subject and said:

"On defence sales, including Harrier, and on the supply of equipment generally, I think that the Chinese will want to move cautiously, and to consider their needs and their resources very carefully before making or accepting any particular proposals. They indicated that they looked to the United Kingdom as a major supplier in the future; ... I did not go to negotiate any specific contracts, but I am confident that the understandings I reached laid the best possible foundation for the further development of trade". (Col. 66-68).

11. The Defence Budget (Chapter 5)

In a Written Answer on 15th April, Mr. Pym said:

"As a proportion of GDP, defence expenditure according to the NATO definition is expected to increase from 4.9 per cent in 1979-80 to 5.1 per cent in 1980-81 (Col. 580). (Figure 21 on page 86 of the White Paper refers).

T H E S E L E C T C O M M I T T E E

12. The Secretary of State appeared for the first time before the House of Commons Select Committee on Defence on 17th April. The Committee's report of this interview is expected to be available before the Debate.

D E C I S I O N S A H E A D

13. A number of important decisions are still to be made. These include:

- a. The replacement of Polaris (211) which, it is understood, is also being examined by the Select Committee.
- b. GLCM basing (216)
- c. Tank Improvements (709 b), and the next generation of ATGW (709 c)

.....

- / d. The Royal Dockyards (755)

- d. The Royal Dockyards (755) on which the results of a study are to be submitted to the secretary of State shortly.
- e. Harrier improvement (715 d)
- f. The response to the Soviet chemical warfare threat. (106,707)

THE MAIN THEME

14. Addressing the Parliamentary Defence Committee on 2nd April, Mr. Pym said that his aim was to establish stability and continuity in defence policy and to strive for steady improvement and growth. He said that the 3 per cent increase in defence spending was "no bonanza" and that it would largely be absorbed in the cost of more sophisticated equipment - hence the need for a continuing "war against waste". His top priority would remain the morale of the Services.

Conservative Research Department,
32, Smith Square,
London, S.W.1.

CPAJ/FJVB
24th April, 1980

LABOUR'S LEGACY1. Labour's Defence Cuts

During their term of office, the Labour Government spelt out the growing Russian/Warsaw Pact threat in all five of their defence White Papers. Yet undeterred by severe warnings from their own professional advisors, from our NATO allies, from a Select Committee and from the Opposition, they cut defence spending by the staggering total of nearly £12,000 million, from 1975-6 to 1983-4.

2. The Cumulative Effect.

a. In September 1977, Dr. Luns, NATO's Secretary General issued a stern rebuke about the cumulative effects of Labour's cuts - pointing out that successive cuts had been made in the minimum level of defence which the Government's own Defence Review had sought to establish.

b. Within their appalling record on defence generally, six areas can be highlighted:

- Weakening our front line forces and our contribution to NATO.
- Blinkered strategic approach (eg: ignoring the threat to our raw materials and trade routes).
- Armed Forces pay - their failure to restore comparability as early as possible.
- Defence-based employment - reduction of jobs and job opportunities.
- The nuclear deterrent - failure to plan for replacement of Polaris.
- Mutual and Balanced Force Reductions (MFBR) - unilateral reduction of Britain's Armed Forces with no quid pro quo.

3. A Bogus Formula.

The Labour Government sought to justify its cuts on the futile argument based on the proportion of our GNP that we spend on defence in relation to that spent by our allies - ignoring the reality that they themselves were responsible for the low level of that GNP and that on the basis of per capita spending (the only true gauge of relative defence spending) we now lag behind the US, France, Germany, Belgium, the Netherlands and Norway. (11SS, "The Military Balance 1979-80, p.94).

4. Labour's Manifesto.

In their 1979 Election Manifesto, Labour said:

"We shall continue with our plans to reduce the proportion of the Nation's resources devoted to defence, so that the burden we bear will be brought into line with that carried by our main allies".

This would have reduced defence expenditure as a proportion of GDP from 4.7% nearer to that of our main

allies (eg: FRG 3.3%, France 4.0%, NL 3.4%, Belgium 3.3%, US 5.0% - thus reflecting the proposal in Labour's Programme 1976 for further cuts of around £1,000 million a year at 1974 prices - which Mr. Mason, when Defence Secretary, admitted would entail,

"At best... a policy of neutrality, at worst it would be surrender".
(Hansard, 13th July 1976, Col. 356).

20



12 DOWNING STREET,
S.W.1.

V
MS

With

The Private Secretary's

Compliments



Defence

MINISTRY OF DEFENCE
MAIN BUILDING WHITEHALL LONDON SW1
Telephone 01-~~924 7022~~ 218 6169

D/S of S/PS 2 (PQ 1400 C)

23rd April 1980

My dear Murdo,

We spoke yesterday about the Motion to be tabled for the Defence Debate on 28th and 29th April.

My Secretary of State feels that the Defence White Paper should stand on its own without (as was the practice under the previous Administration) a detailed Motion. He proposes, therefore, to revert to the practice of the previous Conservative Government and simply move:

"That this House approves the statement on the Defence Estimates 1980, contained in Command No 7826".

I presume that there is no need for the Motion to refer to the two volumes of the Command paper as 7826-I and 7826-II?

I would be grateful if you would arrange for this Motion to be tabled in Mr Pym's name.

I am copying this letter to Petra Laidlaw in the Chancellor of the Duchy's office.

Yours and

D T PIPER

(D T PIPER)
APS/S of S

Murdo Maclean Esq



22 APR 1890

Published Papers

The following published paper(s) enclosed on this file have been removed and destroyed. Copies may be found elsewhere in The National Archives.

Cmnd. 7826-I Defence in the 1980s: statement on the Defence
Estimates 1980, volume 1
Published by HMSO, 2 April 1980

Signed *A Wayland* Date *25 February 2010*

PREM Records Team



Defence 4
MINISTRY OF DEFENCE

MAIN BUILDING WHITEHALL LONDON SW1A 2HB

Telephone 01-218 ^{2111/3} (Direct Dialling)

01-218 9000 (Switchboard)

MO 8/2/12

28th March 1980

Ann Whitmore

Dear Clive,

I attach for your information a copy of the 1980 Statement on the Defence Estimates, which this year has been produced in two volumes. It is being published at 1130 next Wednesday.

Yours sincerely

David
(D B OMAND)

Private Secretary

C A Whitmore Esq

28 MAR 1980

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CC FCO Defence MS
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10 DOWNING STREET

From the Private Secretary

17 March 1980

UK Military Training Assistance Scheme

The Prime Minister has read with interest your letter to me of 11 March on the UK Military Training Assistance Scheme and its attached tables. She has commented that we are not selling enough military equipment overseas.

I am sending copies of this letter to John Wiggins (H.M. Treasury), George Walden (Foreign and Commonwealth Office) and David Wright (Cabinet Office).

M. O'D. B. ALEXANDER

D.B. Omand, Esq.,
Ministry of Defence.

CONFIDENTIAL

9

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Weekend Box 4



MINISTRY OF DEFENCE
MAIN BUILDING WHITEHALL LONDON SW1
Telephone 01-~~938X000~~ 218 2111/3

Prime Minister (2)

MO 24/4

11th March 1980

MO.
A useful survey.
We aren't selling
anything like
enough. *Paul*
Jean Michael,

UK MILITARY TRAINING ASSISTANCE
SCHEME (UKMTAS)

In your letter of 18th February you said that the Prime Minister had asked for a breakdown of UK arms sales in relation to our military training programmes, following sight of the Foreign and Commonwealth Secretary's minute of 13th February to the Chancellor about UKMTAS. I attach tables showing the value of our defence sales over the last few years to those countries who are now or in recent years have been given Service training subsidised in whole or in part by UKMTAS funds, on FCO Votes. The list of 56 such countries does, in fact, include the majority of countries whose Servicemen are trained in MOD establishments or to whom the UK has sold defence equipment.

The attached breakdown of our defence sales has been expressed in constant 1975 prices in order to reflect as far as possible the volume of business done. The full statistics are I am afraid available only for the past six years. The volume of training has been shown in student weeks of training provided, including both training subsidised by UKMTAS and that paid for by the overseas Government: student weeks are a useful indicator of the volume of training, but this measure does not of course discriminate between types of training (which vary from basic infantry skills to the Royal College of Defence Studies).

To assist comparison between the figures for sales and student weeks of training we have provided a summary table covering the six year period and which provides a "league table". It also shows whether British personnel on loan served in the country concerned, the figures being expressed in terms of "loan service personnel years". The summary

/table

Michael O'D B Alexander Esq

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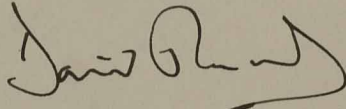
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table shows, as you would expect, that there is a tendency for countries which are high in the league table for sales also to be major recipients of training; and many countries who have bought little have also received a relatively small amount of British training over the period. There are several notable exceptions however and it would be wrong to try to deduce too much from these figures, or from the more detailed annual breakdown given in Tables 1 and 2 attached. Only a small proportion of MOD training is specifically sales-related (i.e. training to support the sale of a product). Occasionally, we relate our agreement to the provision of training to the procurement of particular equipment. Generally however the arrangement of training for foreign servicemen, and the promotion of sales of defence equipment produced by British industry and the Royal Ordnance factories, are quite separate activities. There will be several factors determining whether the country buys British equipment, not least being quality, price and credit terms and HMG's willingness to sell. We do train some overseas servicemen who will be in a position to influence their countries decisions on arms procurement (particularly students at the Royal College of Defence Studies) although in most cases this influence would in fact not arise until many years later.

We regard it as to the advantage to our defence sales to expose the maximum number of foreign Servicemen to British products used by our own armed forces. Experience of British training appears almost always to encourage greater interest in British equipment and this may sometimes tip the balance in favour of an individual sale. It is for this reason of course that defence sales potential and the record of past sales are factors taken into account in determining which countries should be offered training places in MOD establishments.

I am sending copies of this letter to the recipients of yours.

Yours sincerely,


(D B OMAND)

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DEFENCE SALES AND UK TRAINING, 1974-79

<u>Country</u>	<u>UK Defence Sales</u> (£M at Constant (1975) Prices)	<u>Training in UK</u> (Student Weeks)	<u>UK Loan</u> <u>Service Personnel</u> (LSP Years)	<u>Position in League Tables</u> <u>Sales</u>	<u>Position in League Tables</u> <u>Training</u>
Afghanistan	-	446	-	-	38
Algeria	3.338	456	-	30	37
Argentina	47.952	2,591	6	11	21
Bahamas	6.374	777	15	26	32
Bangladesh	4.068	2,067	18	28	24
Barbados	-	279	-	-	46
Belize	0.061	414	23	43	40
Botswana	2.133	724	-	33	33
Brazil	25.662	3,005	8	13	19
Burma	-	596	-	-	35
Chile	7.622	4,616	8	24	14
Ecuador	53,080	947	-	9	29
Egypt	601.752	5,313	-	1	13
Ethiopia	-	329	-	-	43
Fiji	-	300	4	-	45
Gambia	-	206	-	-	50
Ghana	3.437	15,051	22	29	7
Guyana	3.038	2,297	-	32	22
India	569.438	3,530	-	2	17
Indonesia	24.934	653	-	14	34
Iran	566.471	53,574	344	3	3
Iraq	79.045	4,606	-	7	15
Jamaica	-	11,478	1	7	8
Jordan	163.931	20,080	-	4	5
Kenya	110.193	32,155	53	6	4
Korea	6.118	162	-	-	53
Lebanon	8.005	1,959	-	27	27
Lesotho	1.717	3,847	-	22	25
Malawi	3.087	88,635	14	36	51
Malaysia	21,002	-	88	15	16

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DEFENCE SALES AND UK TRAINING, 1974-79

Country	UK Defence Sales (£M at Constant (1975) Prices)	Training in UK (Student Weeks)	UK Loan Service Personnel (ISP Years)	Position in League Tables Sales	Training Tables
Mauritius	-	313	12	-	14
Morocco	14.127	496	-	18	36
Nepal	1.266	906	4	38	30
Nigeria	54.829	113,029	140	8	1
Oman	142.787	8,270	1,098	5	9
Pakistan	7.601	15,130	-	25	6
Philippines	7.707	277	-	23	47
Portugal	1.311	864	-	37	31
Senegal	0.159	29	-	42	54
Seychelles	-	10	2	-	55
Sierra Leone	0.336	5,454	-	40	12
Singapore	1.909	5,504	62	35	11
Spain	13,413	340	-	19	42
Sri Lanka	0.677	2,132	-	39	23
Sudan	11.386	3,426	49	20	18
Swaziland	0.224	165	-	41	52
Syria	36.031	7	-	12	56
Tanzania	19,036	388	-	16	41
Thailand	16,307	2,851	-	17	20
Trinidad	-	1,236	-	-	27
Tunisia	2,122	222	-	34	49
Turkey	-	1,197	-	-	28
Yemen Arab Republic	-	250	-	-	48
Yugoslavia	52.842	434	-	10	39
Zaire	-	1,909	-	-	26
Zambia	9.320	5,981	-	21	10

Note This list of countries includes only those who now, or over the past six years, have received training in MOD establishments funded in whole or in part by UKMTAS funds on FCO Votes.

CONFIDENTIAL UK EYES B

UK DEFENCE SALES IN £M AT CONSTANT (1975) PRICES

	1974	1975	1976	1977	1978	1979	TOTAL
Afghanistan	-	-	-	-	-	-	-
Algeria	NIL	1.600	1.176	NIL	NIL	0.562	3.338
Argentina	1.995	NIL	8.457	0.473	2.949	34.078	47.952
Bahamas	NIL	NIL	3.496	2.878	NIL	NIL	6.374
Bangladesh	NIL	NIL	2.037	1.899	NIL	0.132	4.068
Barbados	-	-	-	-	-	-	-
Belize	NIL	NIL	NIL	NIL	NIL	0.061	0.061
Botswana	NIL	NIL	0.044	0.993	0.329	0.767	2.133
Brazil	4.465	10.290	0.196	2.829	6.636	1.246	25.662
Burma	-	-	-	-	-	-	-
Chile	NIL	3.108	2.750	0.712	0.267	0.785	7.622
Ecuador	43.808	0.880	1.301	6.248	NIL	0.843	53.080
Egypt	NIL	63.865	58.049	159.777	312.799	7.262	601.752
Ethiopia	-	-	-	-	-	-	-
Fiji	-	-	-	-	-	-	-
Gambia	-	-	-	-	-	-	-
Ghana	1.390	NIL	NIL	2.047	NIL	NIL	3.437
Guyana	NIL	1.850	1.028	NIL	NIL	0.160	3.038
India	1.585	5.229	6.898	5.831	518.004	31.891	569.438
Indonesia	0.028	0.040	2.719	1.309	20.606	0.232	24.934
Iran	190.420	17.201	77.377	103.597	177.876	NIL	566.471
Iraq	1.266	11.900	17.785	10.698	27.052	10.344	79.045
Jamaica	-	-	-	-	-	-	-
Jordan	6.816	4.722	1.773	0.067	NIL	150.553	163.931
Kenya	NIL	0.230	35.339	9.200	61.570	3.854	110.193

CONFIDENTIAL UK EYES B

DEFENCE SALES IN £M AT CONSTANT (1975) PRICES Cont.

	1974	1975	1976	1977	1978	1979	TOTAL
Korea	NIL	0.030	2.904	0.177	1.594	1.413	6.118
Lebanon	5.380	NIL	NIL	NIL	2.060	0.565	8.005
Lesotho	NIL	NIL	NIL	NIL	1.515	0.202	1.717
Malawi	NIL	0.653	0.143	0.984	0.806	0.501	3.087
Malaysia	3.325	NIL	0.044	7.063	5.648	4.922	21.002
Mauritius	-	-	-	-	-	-	-
Morocco	NIL	8.700	2.312	3.056	0.059	NIL	14.127
Nepal	1.266	NIL	NIL	NIL	NIL	NIL	1.266
Nigeria	24.329	6.828	14.569	4.329	2.564	2.210	54.829
Oman	113.796	3.212	20.426	0.575	0.931	3.847	142.787
Pakistan	7.199	NIL	NIL	NIL	0.120	0.282	7.601
Philippines	1.772	3.255	0.426	0.287	1.967	NIL	7.707
Portugal	NIL	1.250	0.012	0.024	NIL	0.025	1.311
Senegal	NIL	NIL	0.159	NIL	NIL	NIL	0.159
Seychelles	-	-	-	-	-	-	-
Sierra Leone	NIL	NIL	NIL	0.180	0.156	NIL	0.336
Singapore	0.165	0.400	0.774	0.570	NIL	NIL	1.909
Spain	NIL	NIL	NIL	7.237	5.389	0.787	13.413
Sri Lanka	NIL	NIL	0.677	NIL	NIL	NIL	0.677
Sudan	0.076	NIL	NIL	10.537	0.773	NIL	11.386
Swaziland	NIL	NIL	NIL	NIL	0.224	NIL	0.224
Syria	NIL	1.300	0.068	1.438	4.348	28.877	36.031
Tanzania	NIL	NIL	13.703	NIL	5.333	NIL	19.036
Thailand	0.259	NIL	0.813	7.901	7.334	NIL	16.307
Trinidad	-	-	-	-	-	-	-

CONFIDENTIAL UK EYES B

DEFENCE SALES IN £M AT CONSTANT (1975) PRICES Cont.

	1974	1975	1976	1977	1978	1979	TOTAL
Tunisia	NIL	2.000	NIL	NIL	0.122	NIL	2.122
Turkey	-	-	-	-	-	-	-
Yemen A.R	-	-	-	-	-	-	-
Yugoslavia	15.570	8.500	1.724	14.581	11.303	1.164	52.842
Zaire	-	-	-	-	-	-	-
Zambia	NIL	NIL	3.540	NIL	5.780*	NIL	9.320

UK DEFENCE SALES
(CONSTANT /1975/ PRICES)
ANNUAL TOTALS (£M)

1974	424.910
1975	157.043
1976	282.719
1977	367.550
1978	1186.114
1979	291.269
GRAND TOTAL	<u>2709.605</u>

Constant price indices taken from the CSO's "MONTHLY DIGEST OF STATISTICS FOR NOV 1979"(Table 15.12 Machinery and Transport Equipment total)

*Paid from FCO funds

Table 2

	CONFIDENTIAL						TOTAL
	TRAINING IN UK						
	1974	1975	1976	1977	1978	1979	
Afghanistan	239	46	-	62	68	31	446
Algeria	182	210	55	3	6	-	456
Argentina	395	776	418	358	432	212	2,591
Bahamas	13	75	6	146	312	225	777
Bangladesh	350	226	273	235	549	434	2,067
Barbados	22	22	56	52	62	65	279
Belize	63	64	21	121	56	89	414
Botswana	-	3	10	54	305	352	724
Brazil	420	947	917	301	246	174	3,005
Burma	229	141	97	53	76	-	596
Chile	1,509	974	705	830	565	33	4,616
Ecuador	84	294	250	155	115	49	947
Egypt	115	2,283	460	652	1,264	539	5,313
Ethiopia	223	4	16	83	2	1	329
Fiji	99	69	17	41	28	46	300
Gambia	3	35	52	75	38	3	206
Ghana	2,519	2,191	1,570	2,081	3,565	3,125	15,051
Guyana	193	269	443	524	486	382	2,297
India	560	633	311	473	340	1,213	3,530
Indonesia	196	92	74	92	124	75	653
Iran	12,197	13,634	14,540	5,463	5,172	2,568	53,574
Iraq	273	830	843	1,085	926	649	4,606
Jamaica	1,345	2,492	3,257	1,825	1,357	1,202	11,478
Jordan	4,332	6,220	3,451	1,952	2,265	1,860	20,080
Kenya	2,955	3,725	3,554	5,794	8,919	7,208	32,155

CONFIDENTIAL

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TRAINING IN UK Cont.

	1974	1975	1976	1977	1978	1979	TOTAL
Korea	40	-	19	55	6	42	162
Lebanon	549	747	321	18	124	200	1,959
Lesotho	-	-	-	-	9	170	179
Malawi	645	649	667	864	609	413	3,847
Malaysia	15,482	15,663	12,683	13,422	16,067	15,318	88,635
Mauritius	34	87	102	46	12	32	313
Morocco	233	159	30	56	18	-	496
Nepal	377	189	189	81	79	31	906
Nigeria	16,162	18,843	20,082	20,669	19,353	17,920	113,029
Oman	400	813	1,647	1,679	1,511	2,220	8,270
Pakistan	2,613	4,872	1,738	1,906	2,243	1,758	15,130
Philippines	90	72	40	14	33	28	277
Portugal	149	43	47	176	197	252	864
Senegal	-	-	-	-	-	29	29
Seychelles	9	-	-	-	-	1	10
Sierra Leone	1,473	1,256	1,243	756	487	239	5,454
Singapore	1,390	915	924	863	753	659	5,504
Spain	-	-	-	-	221	119	340
Sri Lanka	866	203	324	221	334	184	2,132
Sudan	563	524	409	595	673	662	3,426
Swaziland	-	-	3	16	24	122	165
Syria	-	-	-	-	7	-	7
Tanzania	-	-	-	49	173	166	388
Thailand	513	382	354	437	682	483	2,851
Trinidad	40	245	229	119	336	267	1,236

CONFIDENTIAL

TRAINING IN UK Cont.

	1974	1975	1976	1977	1978	1979	TOTAL
Tunisia	65	19	27	65	46	-	222
Turkey	203	132	173	199	248	242	1,197
Yemen [<u>Arab Republic</u>]	116	24	103	7	-	-	250
Yugoslavia	51	71	16	162	134	-	434
Zaire	435	363	278	238	402	193	1,909
Zambia	914	943	1,554	1,194	575	801	5,981
GRAND TOTAL	71,888	83,469	74,598	66,417	72,634	63,086	429,362



MO 24/4

NBP Aych

Am

SECRETARY OF STATE FOR FOREIGN AND COMMONWEALTH AFFAIRS

MILITARY TRAINING ASSISTANCE FUNDS

Yes, please.

Am

Thank you for your minute of 5th March.

2. In the light of all your difficulties, and notwithstanding my own in respect of the Defence Budget which are, as you know, acute, I have looked again at whether I can help; and I am prepared to agree that funds for UKMTAS for the financial year 1980/81 - but not for any further years - should be found from my budget. What I propose is a transfer of £2m. between my cash limit for 1980/81 and yours, with the balance of the short-fall perhaps coming from Civil Aid programmes. I think this is a reasonable approach given that UKMTAS is an FCO programme serving primarily foreign policy objectives. As it is, the transfer can, of course, only be at the expense of items that are required for our defence purposes, which I am sure will be as unwelcome to you as it is to me.

3. This brings me to say that I am not sure we are yet looking at all aspects of this subject in the round; and I am very concerned that we should do so, and that the review that the Lord Privy Seal and I agreed should be undertaken should be mounted urgently, and with sufficiently wide terms of reference. As I understand it, our decisions about which countries should receive subsidized training and assistance, and how much, are taken pragmatically and in response to requests from those countries. This may be the only practicable way, but I would like to be sure that it is, and given the value of these activities, we must, for the future, avoid the uncertainty now surrounding next year's UKMTAS programme; and ensure that our use of UKMTAS funds to subsidize training and our Loan Service personnel is compatible with and supports our other efforts outside the NATO area, for which we must seek to make the most intelligent and cost effective use of our resources overall.

/ 4. ...

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4. I am sending a copy of this minute to the Lord Privy Seal; and, in view of what I have said in paragraph 3 above, copies also go to the Prime Minister and the Chancellor of the Exchequer; and to Sir Robert Armstrong.

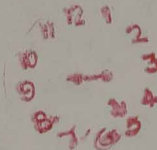
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Ministry of Defence

10th March 1980

CONFIDENTIAL

11 MAR 1960



ICS/80/52

SECRETARY OF STATE FOR DEFENCE

Military Training Assistance Funds

1. During our recent talk we mentioned the problem of the UK Military Training Assistance Scheme (UKMTAS) following the Treasury's rejection of my request for an allocation from the Central Contingencies Reserve.

2. I think we are all agreed that our programme of military training assistance is a very important factor for our defence and foreign policy objectives outside NATO. Unless we can maintain this year's level of assistance in 1980/81, our friends, particularly in South West Asia, Africa and the Caribbean, are unlikely to take seriously our policy of assisting them in building up their own defences. A dramatic drop in the money available for UKMTAS would, moreover, be in stark contradiction to our policy statements since the Soviet invasion of Afghanistan. And we now face the strong likelihood of pressing requests from the government of Zimbabwe for extensive help in establishing and training their new integrated army.

3. I know that you have already talked about this with Ian Gilmour and have considered whether, as an emergency arrangement for the next financial year, you could help us out of MOD funds. I also know that in present circumstances assistance of this kind would be difficult for you and I am sorry to have to raise the matter with you again, but I see no other way.

4. Could you therefore look once more at the possibility of finding £3 million for UKMTAS in 1980/81, as part of your present wider review of defence options into which you may be fitting some additional expenditure for an increased capability outside NATO area. The support we provide to non-NATO countries through this programme is extremely cost effective, and likely to be more expensive than other forms of military assistance.

Defence Dept

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cl B

PS/PS

PS/Mr Howard

PS/PS

Sir A. Adland

Mr P. Moberly.

MW

5. The problem, as we near the beginning of the next financial year, is now very pressing. If you cannot help, we shall have to let a large part of an activity, which we all agree to be very worthwhile, just lapse for 1980/81. For the longer term, as I think you agree, we must set in hand a review of all aspects of our military assistance programme.

(CARRINGTON)

5 March 1980

Foreign and Commonwealth Office

11 MAR 1950



BACKGROUND NOTESTATEMENT ON THE DEFENCE ESTIMATES 1980:DEFENCE IN THE 1980s

1. This year's Defence White Paper is new in format and ambitious in scope. It is divided into two volumes, the second containing a comprehensive collection of statistics on defence. The first volume discusses in a full and open way the underlying principles of our defence effort, the issues and problems facing the Government, and the decisions which have set the guidelines for defence spending not only in 1980 but for several years to come.

The Threat

2. Defence is a means to an end: a response to a threat. SDE 80 analyses the threats Britain and her allies must expect to face in the 1980's, drawing attention to the massive economic and industrial effort that underpins the Soviet military build-up and the way the West's technological lead has been eroded. No motives that the Russians might claim for their acquisition of such massive forces can alter the dangers they present for the West or do away with the need for effective deterrence. The fate of Afghanistan has been a forceful reminder of these lessons.

The Government's Response

3. Britain's defence policy is firmly anchored in our membership of and continued commitment to the North Atlantic Alliance. We have endorsed the aim of increases in the region of 3% a year in real terms in all NATO Allies' defence budgets. We strongly support NATO's Long-Term Defence Programme. Arms control remains an important element of UK and NATO policy, but the prospects for progress have been overshadowed by events in Afghanistan.

4. Chapters 2 and 3 of the White Paper describe the UK's contribution to NATO's nuclear and conventional forces respectively. The Chevaline programme, now nearing completion, to maintain Polaris's effectiveness is mentioned; possible successors to Polaris are being considered. As part of NATO's LRTNF modernization programme, the UK will be providing bases for 160 Ground Launched Cruise Missiles. The rationale for the role our conventional forces play in each area, and the contribution of each of our three Services, is discussed and current problems and corrective measures are explained.

Britain's defence responsibilities and interests in the world at large are covered in Chapter 4. The Government are considering certain improvements to the Services' capability to operate flexibly outside the NATO area, without diminishing the central commitment to NATO itself. Chapter 5 describes other tasks undertaken by the Services, especially their vital, demanding and often dangerous role in Northern Ireland.

Human Resources

5. The men and women in the Armed Forces have been undervalued in recent years; in 1977-80 a disturbing number chose to leave prematurely. The Government's prompt action on pay helped towards a better level of recruiting in 1979-80. The White Paper stresses the Government's continuing commitment to give proper treatment to the Services, in terms both of pay and of conditions of service; to improve recruitment and retention; and also to improve the manning, training and equipment of reserve forces. The role of the Women's Services, including the question of arming women, is discussed and a number of issues affecting the MOD's civilian staffs are examined.

Financial Resources

6. The closing chapters of SDE 80 include a detailed examination of the Government's equipment programme and policy and a frank discussion of the pros and cons of collaboration in the equipment field. Chapter 8 deals with the defence budget itself. Two major themes emerge: the Government's commitment to maintain a proper level of defence expenditure, and the need to achieve the most effective possible use of resources.

7. The defence budget for 1980/81 represents an increase of some 3½% in real terms compared with the expected out-turn for 1979/80. The Government plans a continuing real growth in defence spending up to 1983/4, consistent with NATO's target of 3% per year: in defence, long-term planning and continuity are of the essence. The particular problems posed by the escalating foreign exchange costs are mentioned; the agreement by which the Federal Republic have helped meet the costs of British forces Germany expires this year.

8. Defence spending is not an alternative to spending on other programmes so much as a precondition for them: it allows us to assure the basic security without which the free and peaceful pursuit of our national life would become impossible. But the scale of our general economic capability, and the wider constraints on resources put us on our mettle to achieve the utmost economy in allocating and applying the means at our disposal.



Defence

[Handwritten initials]

[Handwritten signature]

NBOM ?

Treasury Chambers, Parliament Street, SW1P 3AG

[Handwritten mark]

The Rt Hon Francis Pym MC MP
Secretary of State
Ministry of Defence
Main Building
Whitehall
London SW1A 2HB

4/5

4 March 1980

Dear Francis,

CLASS I SUPPLEMENTARY ESTIMATES: EXCESS OVER DEFENCE CASH LIMIT

Thank you for your letter of 21 February about your Supplementary Estimates.

I am grateful for your assurance that you are still pursuing ways of reducing the amount of the potential overspend on your 1979-80 cash limit.

I have noted your comments. I recognise the difficulties of controlling the precise timing of defence expenditure and the considerable achievements which have been attained. But in Opposition and in Government we have emphasised the importance of cash limits. Overspends, particularly if, like yours, they are repeated, bring into question our resolve as a Government to control public spending.

Of course the possibility is not excluded of changes in the present system. But I should be reluctant to contemplate changes which weaken its effectiveness in promoting financial discipline and control, or the restraint of public spending which is central to our policy. Unless and until changes are agreed I must ask you please to ensure that the constraints imposed by the system as it is are accepted by your department.

I am copying this letter to the Prime Minister.

[Handwritten signature of John Biffen]

JOHN BIFFEN

4 MAR 1980



CONFIDENTIAL

Defence ^{JH}



*Top copy on
Econ PSI 74 8
Public expenditure*

10 DOWNING STREET

From the Private Secretary

3 March 1980

Dear Martin.

Public Expenditure White Paper

The Chancellor minuted the Prime Minister on 26 February to the effect that he was now proposing to publish the Public Expenditure White Paper either on Budget Day or the day after the Budget. The Chancellor has since spoken to the Prime Minister about this, and has told her that he intends to publish the White Paper on Budget Day itself. The Prime Minister is quite content.

The Prime Minister has also read Brian Norbury's letter of 26 February, and agrees that the Statement on the Defence Estimates should be published in the week beginning 31 March; and she is content for the Secretary of State for Defence to announce this by means of an early, arranged PQ. She has no objection to the proposal that the Defence debate should take place in the week beginning 14 April; she assumes that this will be settled between the Secretary of State for Defence and the Chancellor of the Duchy.

I am sending copies of this letter to the Private Secretaries to members of the Cabinet, Murdo Maclean (Chief Whip's Office), Charles Cumming-Bruce (House of Lords) and David Wright (Cabinet Office).

in

KHG

Tim Laker.

Martin Hall, Esq.,
HM Treasury

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Defence

*NBPN yoh
Pant - 27/2*

Treasury Chambers, Parliament Street, SW1P 3AG

Rt Hon Lord Carrington PC KCMG MC
Secretary of State
Foreign & Commonwealth Office
Downing Street
London SW1A 2AL

27 February 1980

Dear Peter,

UK MILITARY TRAINING ASSISTANCE SCHEME

I am replying to your minute of 13 February addressed to the Chancellor. I have also seen the letter of 18 February from Number 10 to Francis Pym's Private Secretary, and Francis Pym's letter of 22 February to the Chancellor.

I do not think that we should re-open discussion of a public expenditure programme immediately after decisions have been reached and programme totals have been agreed, for publication in the White Paper.

This item was recorded as an additional bid in 'The Scope for Reductions', but was not mentioned in our bilateral discussions. I note your views on the cost-effectiveness of UKMTAS, and its benefits to the UK. If it is so important, I can only suggest that room be found for it at the cost of things regarded as of lower priority. Alternatively, since Francis Pym agrees that there is a significant benefit to defence policy objectives from UKMTAS, he might be prepared to reconsider the possibility of finding you some money from within the approved Defence Budget: if so, I would have no objection.

But I really cannot accept that UKMTAS should be an exception to the general rule set out in the Chancellor's minute of 6 February to the Prime Minister. In this as in other matters our scope to pursue foreign policy objectives has to be contained within our available resources.

I am sending copies of this letter to the Prime Minister, Francis Pym and Sir Robert Armstrong.

John Biffen

JOHN BIFFEN

27 FEB 1980

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Original on
Econ PD 118
Public Expenditure



MINISTRY OF DEFENCE
MAIN BUILDING WHITEHALL LONDON SW1
Telephone 01-~~9307822~~ 218 2111/3

MO 21/2/25

26th February 1980

Dear Tim, T 26/2

PUBLIC EXPENDITURE WHITE PAPER;
STATEMENT ON THE DEFENCE ESTIMATES, 1980

I have consulted my Secretary of State (who is at present in Germany) about the Chancellor of the Exchequer's minute to the Prime Minister of today.

My Secretary of State has asked me to say that he considers that if the Public Expenditure White Paper is to be published on 26th March, it would make most sense to publish his Statement in the week beginning 31st March, probably on Wednesday 2nd April (shortly after his return from his visit to China); if the Prime Minister is content he would propose to announce this publication date this week by means of an early, arranged, PQ.

April 2/80

If the Statement were published just before the Recess, my Secretary of State would see considerable merit in a defence debate being arranged in the week beginning 14th April (he presently plans to be abroad on another official visit for most of the week beginning 21st April).

I am sending copies of this letter to the Private Secretaries to the Members of OD, the Chancellor of the Duchy of Lancaster, the Paymaster General and the Chief Whip; copies also go to Charles Cumming-Bruce (House of Lords) and David Wright (Cabinet Office).

Yours ever,

Brian Norbury

(B M NORBURY)

CONFIDENTIAL

Zpps



MINISTRY OF DEFENCE
MAIN BUILDING WHITEHALL LONDON SW1
Telephone 01-~~930 7022~~ 218 2111/3

MO 24/4

25th February 1980

Dear Michael,

Lt. Punt 26/2

UK MILITARY TRAINING ASSISTANCE SCHEME

My Secretary of State has now written to the Chancellor of the Exchequer about the request from the Foreign and Commonwealth Secretary for a call on the contingency reserve for military training assistance. This note is just to let you know that we are pressing on the preparation of the information on UK arms sales in relation to our military training programmes you requested in your letter of 18th February. This is not entirely straightforward, and it is taking us a little time to assemble the material.

I am sending a copy of this letter to David Wright (Cabinet Office).

*Yours and
Baroness*

(B M NORBURY)

M O'D B Alexander Esq
10 Downing Street

CONFIDENTIAL

MINISTRY OF DEFENCE
MAJORS BUILDING WITTHAMPTON LONDON SW1



26 FEB 1950
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THE MILITARY TRAINING ASSISTANCE SCHEME

The Secretary of State has now written to the Canadian
Ambassador about the request from the London and
Ottawa Secretaries for a call on the contingency reserve
for military training assistance. This note is just for
you to know that we are proceeding on the basis of the
information on the time scale in relation to our military
training programme you reported in your letter of 18th
February. This is not strictly straightforward, and it
is taking us a little time to assemble the material.

I am sending a copy of this letter to your
(London Office).

(S. H. ROBERTS)

10 Downing Street
London, W.C.2

CONFIDENTIAL



MINISTRY OF DEFENCE WHITEHALL LONDON SW1A 2HB

TELEPHONE 01-218 9000

DIRECT DIALLING 01-2182111/3

MO 24/4

22nd February 1980

Dear Jeffrey

UNITED KINGDOM MILITARY TRAINING ASSISTANCE SCHEME

(UKMTAS)

The Foreign and Commonwealth Secretary sent me a copy of his minute of 13th February on this subject.

I very much agree with him that now would be the worst possible moment at which to cut back drastically on the UKMTAS programme. It is in the interest of the United Kingdom, and the West as a whole, that we should continue to respond helpfully to requests from Commonwealth and other friendly countries for military assistance (training in the UK and the provision of Service personnel on loan). Since the Government took office, we have stressed the global nature of the Soviet threat and the importance we attach to our defence relations with non-NATO countries, in the Middle East, Africa, the Caribbean and elsewhere. Particularly since Afghanistan, we have been seeking to encourage our Allies to take account of the threat to Western interests outside the NATO area. A reduction in our own programme of subsidised military training could thus be most damaging to the achievement of our foreign and defence policy objectives.

I have considered, therefore, whether funds should, exceptionally, be made available for UKMTAS from Defence Votes. I have concluded that no further reduction in the Defence Budget would be feasible or justifiable even for this purpose. That being so, I hope that funds can be made available from the Contingency Reserve, so that we can at least maintain at the present level the UKMTAS programme.

/I am ...

The Rt Hon Sir Geoffrey Howe QC MP

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I am sending copies of this minute to the Prime Minister,
the Foreign and Commonwealth Secretary and Sir Robert Armstrong.

James L. ...

Francis Pym

Francis Pym

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Defence



MINISTRY OF DEFENCE WHITEHALL LONDON SW1A 2HB

TELEPHONE 01-218 9000
DIRECT DIALING 01-218 2111/3

MO 8/2/12

21st February 1980

ms
Dear John,
Mr Lambert
Prime Minister
A. S. S. S.
24/2
(2)

CLASS 1 SUPPLEMENTARY ESTIMATES:
EXCESS OVER DEFENCE CASH LIMIT

Thank you for your letter of 11th February in which you told me that you had approved Supplementary Estimates which will provide an additional £63.8m above the defence cash limit of £8553.6m.

As you know, the increased provision has had to be requested under the present rules because we cannot be sure of eliminating a potential overspend and because the incidence of the economy measures which have been put into effect cannot be forecast precisely. I can, however, assure you, as I have done before, that we have been looking at everything which might reasonably be done. To illustrate this, let me say that we have already imposed a recruiting ban on civilian staff, cut travel and overtime and imposed administrative economies. We have also given very careful consideration to still further cuts in fuel purchases, beyond those which we made earlier. These further cuts would have saved about £15m by reducing naval operational stocks and RAF operational reserves. That is to say there would be a loss, albeit temporary, of potential operational capability. In the present international situation I do not think it appropriate to do this.

/ It ...

The Rt Hon John Biffen MP

CONFIDENTIAL



It is easy to say, with a degree of hindsight, that greater savings might have been made if action had been taken earlier. This is, if I may say so, a greatly over-simplified view. Inflation, and in particular the continued increase in oil prices which alone has added over £100m to our costs in the year, is higher than was anticipated. The effect of this, and of a cash limit which was too tight in the first place, has been to inflict a 3 per cent volume squeeze on the Defence programme. This does limit the room for manoeuvre. Moreover there have been late developments in the Iranian situation which have denied us £34m since the beginning of December 1979 of receipts when it was not possible to find further offsetting savings. Hence my officials have, with my agreement, suggested to yours that an increase in the cash limit would be justifiable on this account.

I should also emphasise the very fine margins to which we are working. Although the sum of £63.8m is large in itself, it represents only $\frac{3}{4}$ of one per cent of the MOD cash limit. It is, as I am sure your officials would agree on the basis of their forecasting experience, within the margin of estimating error. Industry is amazed that we try to work to such a degree of accuracy and within accounting rules which allow no flexibility in the handling of cash flow. When our resources are so closely budgetted, taut programming and estimating inevitably mean steering close to the limit if we are to avoid embarrassing underspends and waste of resources. We do therefore monitor the programme and the cash flow very carefully: indeed I am concerned that much effort goes into this which might more profitably be employed on getting better value for money.

Looking to the future, my Department has put a number of proposals to yours for introducing some greater flexibility in financial year management of cash limits. I understand the reasons which have led you to be very cautious about these ideas, but I do believe that there are procedures which will be effective. I am bound to observe that the damage which you see as accompanying the announcement of my Supplementary Estimates this year must in part be explained by the false

/ expectations...

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expectations which have been generated about our current system. The impression has been given that we can fine tune our expenditure in a single year to match the cash limit exactly and in an efficient way. Under present accounting procedures for the management of major public sector procurement programmes, this is simply not possible and I believe we should recognise the fact. I do therefore very much hope that Sir Derek Rayner can come up with proposals which, whilst maintaining the kind of financial discipline which the cash limit system was designed to inculcate, moderate to some extent the rigidity with which it is currently applied.

I am copying this letter to the Prime Minister.

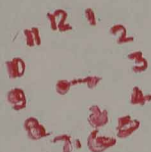
James

Francis

Francis Pym

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MINISTRY OF DEFENCE
MAIN BUILDING WHITEHALL LONDON SW1
Telephone 01-~~938 7022~~ 218 2111/3 2/2

MO 8/2/12

20th February 1980

Dear Tom,

PUBLIC EXPENDITURE ANNOUNCEMENTS

I have shown my Secretary of State your letter to John Wiggins of 20th February; and he has asked me to acquaint you with the problem he is now facing over when he should publish his Statement on the Defence Estimates.

Our plan was that the Statement should be published not before, but very shortly after, the Public Expenditure White Paper (I attach a relevant extract from Volume 1) but that was on the basis that publication would be possible in the week beginning 17th March. If the publication of the Public Expenditure White Paper was deferred until the following week it presently seems that since my Secretary of State will be abroad on an official visit that week he would need to publish in the following week (beginning 31st March), perhaps most desirably on 2nd April. The alternative, to which there are a number of objections, would be to publish the Statement before, instead of after, the publication of the Public Expenditure White Paper. My Secretary of State wanted you to be aware of these considerations.

I am sending copies of this letter to John Wiggins (and also to Alastair Pirie to whom I wrote, coincidentally, on this subject earlier today) and to the Private Secretaries to the Chancellor of the Duchy of Lancaster, the Chief Whip, the Paymaster General and the Secretary of the Cabinet.

Yours and
B M Norbury

(B M NORBURY)

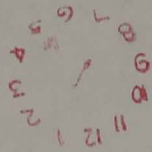
T P Lankester Esq
10 Downing Street

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8 The Defence Budget

801. The defence budget in 1980/81 will total £8,061 million at 1979 Survey prices. This represents an increase of some 3½% in real terms compared with expected out-turn for 1979/80. In 1981/82 and the two following years the Government plans continuing real growth in defence spending consistent with the NATO target of 3% each year, producing defence budget levels of £8,243 million, £8,490 million and £8,745 million. Volume II of this statement contains a number of analyses comparing the provision in Defence Estimates in 1980/81 with previous years.

Figure 19 Division of the Defence Budget (1980/81) by the Principal Headings



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18 February 1980

UNITED KINGDOM MILITARY TRAINING ASSISTANCE SCHEME

The Prime Minister has seen the Foreign and Commonwealth Secretary's minute of 13 February to the Chancellor of the Exchequer on this subject. She has asked for a breakdown of U.K. arms sales in relation to our military training programmes over the years. I should be grateful if you could let me have an analysis covering the last decade.

I am sending copies of this letter to John Wiggins (HMT), George Walden (FCO) and David Wright (Cabinet Office).

M. O'D. B. ALEXANDER

Brian Norbury, Esq.,
Ministry of Defence.

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CHANCELLOR OF THE EXCHEQUER

*Any I have a
break down of
from calls in relation to
military training
overseas
years?
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Prime Minister

Am

United Kingdom Military Training
Assistance Scheme (UKMTAS)

1. The subsidised help we give through UKMTAS to foreign governments in the training of military personnel in this country is an extremely valuable and cost-effective instrument of overseas policy. But on present plans, and on the basis of the 1979 PESC prices, there will be little more than £1.6 million for UKMTAS in 1980/81, compared with £6.4 million this year. This is a savage drop. I would regard it as a serious setback if we cannot maintain the UKMTAS Vote at least at current cash levels.

2. Pound for pound I can think of no other form of assistance which stands us in such good stead with countries in the third world. The Ministers of State in the Foreign and Commonwealth Office dealing with these countries are emphatic in saying how highly our help is valued. The training we give in the UK to their servicemen is, of course, a form of pump-priming for sales of defence equipment. But much more than that, it directly contributes to the effectiveness of local forces in areas of the world where stability is an essential safeguard of British interests and those of the West generally. The aim is to help these countries to help themselves in improving their security and a small investment in training can bring us a dividend out of all proportion to its cost. This would be the worst possible moment at which to cut back drastically on the programme.

/3.

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3. This applies above all to countries like Pakistan where we have a particular interest in assisting the local forces to stand on their own feet in the face of a growing threat, whether external or through subversion. When I visited Islamabad, I was able to offer the Pakistanis an immediate doubling of our military training subsidy for the remainder of this financial year, a gesture which was warmly appreciated. But as things are now, we cannot possibly maintain this kind of effort in 1980/81. To take another example: King Hussein has recently asked for help with restructuring the retraining the Jordanian Forces in connection with our sale of tanks to Jordan; yet there is no prospect of our being able to subsidise training courses for this here under present plans. It is a similar story elsewhere in the Middle East, in the Caribbean, in South East Asia, with the Commonwealth countries of Southern Africa and in Rhodesia where we ought to be providing funds for training the army of the new Zimbabwe.

4. We face the prospect of so large a change in the UKMTAS programme in 1980/81 compared to this year largely through a technicality. The previous government decided to triple spending on UKMTAS in the current financial year and the money was found to enable us to bring the training programme up to its present level. But the PESC figure remained unchanged, so that all our subsequent discussions about cuts in government expenditure were based on the old PESC figure before the UKMTAS Vote was tripled. Your officials have the details.

5. I have, of course, looked at every possible way of finding funds in other FCO Votes to cover a shortfall of some £4.1 million if we are to maintain our current effort. There are very strong reasons against diverting money from the Aid Programme, not just because the cuts already imposed

*- lets see the result of the election -
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there have left no room for further pruning, but because of the protests we would certainly face in Parliament and elsewhere if money for economic development and similar purposes were switched to military training. There is no way in which I could find anything like £4 million by savings elsewhere in FCO spending, although we might be able to find up to £0.7 million in 1980/81 provided there is no slippage in our 1979/80 programme of military aid for Belize and Zambia.

6. I conclude that the only possible way of finding the remaining £3.4 million for 1980/81 is from the Central Contingencies Reserve. The amount is small but the need in my view is pressing for the reasons I have given. It really is very important not to disappoint our friends over this.

7. We are now entering the second stage of the Western response to the Soviet invasion of Afghanistan. That stage will to a large extent consist of working out plans to help shore up our friends in the troubled area, Turkey and Pakistan and perhaps others. These plans will almost certainly be very expensive. I am very conscious that, as ~~the Chancellor~~ ^{you} of the Exchequer pointed out in ~~his~~ ^{your} minute of 6 February ~~to you~~, our poor economic circumstances make it hard for us to take a lead in this phase, and we are likely to lag somewhat behind the Germans and French when the hat goes round. But I regard it as inconceivable after all that we have said that we should not bear some part of the burden. It may well be that a modest programme of military training and assistance would be a good contribution for us to make. It will not head off the inevitable requests for further massive economic aid to Turkey and others, but it might help us to cope with such requests within our means.

8. I am sending copies of this minute to the Prime Minister, the Secretary of State for Defence and Sir Robert Armstrong.

C

13 February 1980

(CARRINGTON)

Foreign and Commonwealth Office
CONFIDENTIAL

13 FEB 1980



Clegg JMS

to see

Prime Minister Defence ²

MOD or likely to
 over-spend for the second
 year running.

Treasury Chambers, Parliament Street, SW1P 3AG

R
11/2

Rt Hon Francis Pym MC MP
 Secretary of State
 Ministry of Defence
 Main Building
 Whitehall
 London SW1A 2HB

11 February 1980

Dear Francis,

CLASS I SUPPLEMENTARY ESTIMATES : EXCESS OVER DEFENCE CASH LIMIT

Your Department has submitted Spring Supplementary Estimates on Class I Votes 1 and 2 which, taken together with the Supplementary on the PSA's Vote 4 bring you £63.8 million over the defence cash limit of £8553.6 million. It is not a technical matter of additional provision in certain votes, to be offset by savings in others within the cash limit. It will therefore be necessary to inform Parliament, by a note in the Supplementary Estimates, that the need for them arises because the previously announced cash limit is expected to be overspent. This follows the procedure in certain other cases where an overspend is now in prospect, but of much smaller amounts.

I see no alternative under the present Parliamentary rules but to submit the Supplementaries to Parliament so that the risk of an Excess Vote is eliminated. But it is really most unfortunate that we should have to do this, and so announce the prospect of a substantial overspend of the defence cash limit, for the second year running, in contravention of the general policy on cash limits to which we as a Government rightly attach high importance. I am well aware of the difficulties of controlling defence expenditure at the margin, and of the adverse impact of certain contingencies, like Iran. I recognise too the efforts now being made by your department to keep within the cash limit. I sincerely hope that they will be successful. That would help to mitigate the damage caused by the announcement of the Supplementaries. But strict observance of cash limits is a central feature of our general policy, and the announcement of the supplementaries will itself be damaging.

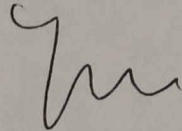
In so far as the final outturn does show an excess over the cash limit it will of course have to be offset by at least a commensurate cut in the cash limit for 1980-81.

I must ask you once again to consider how to avoid this sort of thing happening yet again. The history of this year suggests that the present situation could have been avoided had remedial action been taken sooner. You and I exchanged letters after the excess emerged at the end of last year. When we met on 21 September you agreed that the integrity of the limits must be preserved. In October I wrote to you expressing concern at the way in which your expenditure seemed to be running ahead of plan and you assured me, in your letter of 13 December, that you were making every effort to contain the outturn within the cash limit. It is much to be regretted that the risk of failure is now such that we have to ask Parliament for these Supplementaries.

attached

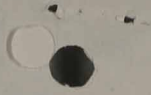
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I am sending a copy of this letter to the Prime Minister.



John Biffen

JOHN BIFFEN



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Defence 2. 8



MINISTRY OF DEFENCE
MAIN BUILDING WHITEHALL LONDON SW1
Telephone 01-~~830 7800~~ 218 2111/3

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MO 8/2/12

5th February 1980

Dear Clive,

X

I am sending you separately for the record my Secretary of State's comments on Martin Hall's letter of 4th February about the agreement reached on future defence budgets in the PESC period. Mr Pym has also asked me to send you this personal note relating to his conversation with you.

A cardinal feature for my Secretary of State of the agreement reached last week was that it enabled him to give effect to the Prime Minister's intention to aim for an increase in real defence spending of in the region of 3% in line with the agreed NATO target. When Mr Pym discussed this with the Prime Minister they were both in agreement that this aim should be preserved if at all possible. It follows therefore that if it turns out that a shortage of cash next year is likely to push us off the NATO target then it is only right that the situation should be reviewed by Ministers, and this would be my Secretary of State's firm intention.

Prime Minister.

Yours ever,

Jair

I shall not bother you with the correspondence mentioned at X/ above which is an exchange between the Treasury and the MOD putting their own glosses on the agreement on the defence budget which the Chancellor and Mr Pym accepted last week. Fortunately, it does not unravel the agreement. But I thought you should be aware of the second paragraph above since it refers to your private conversation with Mr Pym. Personally, I don't think we can object to the last sentence: if the work which takes place in this system, Mr Pym is bound to ask for it to be reviewed.

Clive Whitmore Esq
10 Downing Street

SECRET

Defence
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MINISTRY OF DEFENCE
MAIN BUILDING WHITEHALL LONDON SW1
Telephone 01-~~936 7022~~ 218 2111/3

MO 8/2/12

5th February 1980

Dear Sir,

DEFENCE BUDGET 1980/81 - 1983/84

As you know, the Secretary of State for Defence is content with the formulation of the agreement on future Defence Budgets set out in the enclosure to your letter of 30th January. He has, however, just seen a copy of Martin Hall's letter to you on 4th February commenting on the agreement.

The Defence Secretary has asked me to say that his understanding of the agreement which was reached last week is that the agreed wording means what it says; in particular the agreement says that the defence cash limit will be subject to review next year, in the light of economic and international circumstances, with a view to aiming for an increase in real terms of in the region of 3% in line with the agreed NATO target. It follows therefore that the prospect of our achieving such a 3% real increase in the Defence Budget must be an integral element in the review of the cash limit.

I am sending copies of this letter to the recipients of yours.

Yours ever,
David Omand

(D B OMAND)

C Whitmore Esq
10 Downing Street

I discussed his letter with Mr Hall's
5th February with Mr Omand and Mr Hall,
and we all agreed to have the correspondence
done in new notes.

PLS
6 in'

SECRET

6.



Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

4th February, 1980

Do Aive,

DEFENCE BUDGET 1980/81 - 1983/84

Thank you for your letter of 30th January about the agreement reached with the Defence Secretary. I confirm that the Chancellor is content with the formulation of the agreement set out in the enclosure to your letter.

I ought for the record also to confirm that, given the formula in paragraph 1(ii) of your annex, it is his understanding that the existence of the NATO 3 per cent target will not per se be adduced as a sufficient reason for review of the MOD cash limits during the course of the next financial year.

I am sending copies of this letter to the other recipients of yours.

L aw,

MA

(M.A. HALL)
Private Secretary

C. Whitmore, Esq.,
Private Secretary,
10, Downing Street

18 FEB 1960



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Original - G/R
CDHOS

VEB

CF to note

10 DOWNING STREET

THE PRIME MINISTER

4 February 1980

Dear Mr. Soutwell

Thank you for your letter of 8 January on defence expenditure.

Determining the defence budget must start from considerations of what is needed for national security although of course a judgement has finally to be made on the basis of what the nation can afford. The nation's security is the first responsibility of any government. We must, therefore, ensure that our forces, together with those of our NATO allies, are adequate to deter aggression on whatever scale it may be threatened, conventional, theatre nuclear and strategic nuclear. The recent decision by the Alliance to modernise its theatre nuclear forces in the face of the introduction by the Soviet Union of large numbers of formidable new weapons like the SS20 missile and Backfire bomber, and the Government's determination to maintain the effectiveness of our strategic nuclear deterrent must be seen against this background.

We intend to pursue practical, realistic and balanced measures of arms control and disarmament which will reduce the level of military confrontation in Europe and secure a more stable East-West relationship. An arms control offer to the Soviet Union to negotiate on the limitation of long-range theatre nuclear weapons was an integral part of the Alliance's modernisation decision. However, the Russians have rejected this offer. Their invasion of Afghanistan has underlined their readiness to use their massive military strength where they think the risks are justified, and the need for NATO accordingly to maintain a credible deterrent.

/ As you

As you acknowledge it is a central objective of our economic policy to bring down the rate of inflation. To that end we are also determined to reduce the total level of public spending. But within the total we must make judgements about priorities and we have decided that spending on defence must have priority because of the needs of national security. The effects of defence expenditure on inflation are unlikely to be significantly different from those of other public expenditure on goods and services. What really matters is how public spending is financed. In the 1970s, for example, defence expenditure was being reduced both in real terms and as a share of the national income. But we had mounting public sector deficits, too much of which was financed by printing money; and as a result we had mounting inflation. We are determined to overcome the cancer of inflation by progressively reducing the burden of public sector financing.

There is no reason why we should not achieve this while at the same time strengthening our defence capability.

Yours sincerely
Raymond Stelmach

D. H. Southall, Esq.

Qualitas Peace & Service

SECRET



Defence

5

10 DOWNING STREET

From the Principal Private Secretary

30 January 1980

DEFENCE BUDGET 1980/81-1983/84

I attach the form of words on defence expenditure which you, David Omand and I discussed at length yesterday. You told me yesterday evening that this was acceptable to the Chancellor of the Exchequer, and David Omand similarly confirmed that the Defence Secretary agreed to it.

I understand that you and the Ministry of Defence have since reached agreement on what should be said about defence expenditure in the Chancellor of the Exchequer's paper on public expenditure which is to be discussed at Cabinet tomorrow.

I am sending a copy of this letter and of the attachment to David Omand (Ministry of Defence). I am also sending copies to John Chilcot (Home Office) and David Wright (Cabinet Office).

G. A. WHITMORE

Martin Hall, Esq., M.V.O.,
HM Treasury.

SECRET

SECRET

DEFENCE BUDGET 1980/81-1983/84

The Ministry of Defence's cash limit for 1980/81:-

- i. will be raised as necessary to cover the cost of the Government's decisions on the recommendations of the Armed Forces Pay Review Body; and
- ii. will otherwise be on the same basis as the cash limits decided for other public expenditure programmes but subject to review in the light of economic and international circumstances, with a view to aiming for an increase in real terms of in the region of 3% in line with the agreed NATO target.

As a contribution towards the measures necessary for a major reduction in public expenditure in 1980/81, the Defence Secretary will carry out measures to achieve a reduction in defence spending of £62m. The planned figure of £8062m published in Cmnd 7746 for 1980/81 will be reduced to £8000m at 1979 Survey prices.

The figures for the later years, including provision for Polaris replacement costs, will be £8240m in 1981/82, £8487m in 1982/83 and £8742m in 1983/84.

SECRET

CONFIDENTIAL

Ref. A01265

PRIME MINISTER

Statement on the Defence Estimates 1980

(C(80) 8)

BACKGROUND

Since OD discussed and generally approved the draft Statement on the Defence Estimates 1980 on 22nd January a number of amendments have been made. Some of these reflect points made in that discussion; others are editorial. One aim of the discussion at Cabinet of the Statement will be to ensure that everybody is content with the amendments. Another will be to allow those members of Cabinet who are not members of OD some insight into what is going on in the defence field; this is almost the only occasion in the year at which that is possible.

HANDLING

2. You will wish to invite the Secretary of State for Defence to introduce the Statement. The ensuing discussion should cover the following points:-
- (a) Following a suggestion at OD, paragraph 3 of the introduction and paragraph 108 now refer to the Afghanistan situation. Is it agreed that these references suitably relate the Statement to the current crisis in world affairs?
 - (b) Paragraph 123 of the Statement has been amended to remove the references in the original paragraph 122 to "controlled escalation", which was one of the NATO cliches about which you expressed doubt at OD on 22nd January. Other cliches such as "flexible response" and "forward defence" remain e. g. in paragraph 120. As before, they are explained (paragraphs 121-122). Are you content with this?
 - (c) Paragraphs 130-135, on Arms Control, have been amended in the light of the Foreign and Commonwealth Secretary's suggestions. Is he now content?

CONFIDENTIAL

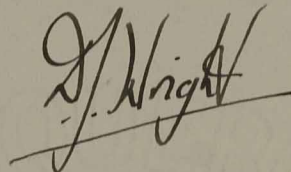
- (d) Paragraph 211 on Chevaline (the Polaris improvement programme) is still in square brackets. This is new since OD, but largely reflects what the Secretary of State for Defence said in the nuclear debate on 24th January. Does the Secretary of State for Defence want this paragraph in or out?
- (e) In regard to "Wider Defence Interests" in Chapter 4, you may care to mention that the Secretary of the Cabinet has set in hand an interdepartmental study of the political and economic case for a United Kingdom military intervention capability outside the North Atlantic Treaty Organisation area in the light of changes in the international situation. The Secretary of State for Defence has been invited thereafter to examine the feasibility and cost of providing that intervention capability, and the implications of doing so for the other four main elements of defence policy.
- (f) Paragraphs 502-509 on Northern Ireland have been discussed between the Secretary of State for Defence and Secretary of State for Northern Ireland. A revised draft of paragraph 502 was circulated to members of OD by the Secretary of State for Defence's office on 25th January. This draft, incorporating two amendments you suggested (Mr. Alexander's letter to the Ministry of Defence of 28th January), is annexed herewith. We have asked MOD to circulate it to all members of the Cabinet. Do they agree with it?
- (g) Paragraph 803, on the Defence Budget, talks about "our economic strategy of reducing public expenditure for the time being". At OD on 22nd January the Chancellor of the Exchequer emphasised that our economic strategy is to reduce public expenditure to a sustainable level. Is the Chancellor of the Exchequer content with this revised draft?
- (h) The figures for the Defence Budget, in Chapter 8 and elsewhere, are still blank. You may wish to explain that they will be filled in when the Cabinet has completed its public expenditure exercise.

CONFIDENTIAL

3. You could in theory also mention that the Secretary of State for Defence has in hand an urgent study on the priority to be accorded to the four main elements of defence policy (nuclear, United Kingdom base, forces in Germany and Atlantic/Channel) in the light of fears expressed by OD in December that manpower and financial resources might not be adequate to sustain all four. But it might be wiser not to mention this large subject to the whole Cabinet, who (unlike OD) will not be shown the results.

CONCLUSION

4. The Cabinet should agree that the Statement be published on 27th February, subject to final editing which should take account of points made in the discussion.



p.p. (Robert Armstrong)

29th January, 1980

Revised Passage on Northern Ireland

"502. The Government's purpose is to restore normal life to the people of Northern Ireland. Removing the constant threat of violence is a first priority and vital to this is the work of the Services - demanding, often tedious and always dangerous. We look forward to a time when troops in Northern Ireland, while remaining immediately available to assist the Civil power, can concentrate on training for their primary role in war. Already in many areas the Royal Ulster Constabulary can handle the bulk of the anti-terrorist task without military assistance. But in other areas a more active Army role remains essential. Much of their work in support of the RUC is necessarily spent on patrolling, whether in city streets or in open countryside, on checkpoints and on static guard and observations duties. But, since they are a prime target for terrorist attack, commanders take continual care that only necessary operations are undertaken. Great responsibility devolves upon junior NCOs and on individual soldiers. These duties, particularly searches of people and their vehicles, demand high levels of concentration, tact and sensitivity towards the community."

SECRET

4



MINISTRY OF DEFENCE
MAIN BUILDING WHITEHALL LONDON SW1
Telephone 01-930 7022 218 2111

MO 8/2/12

29th January 1980

Dear Clive,

Following his discussion with the Prime Minister this morning, after which I understand that he had a word with you, my Secretary of State has asked me to let you have the enclosed piece of paper, which is the one to which he was referring. In conveying the substance of the Prime Minister's discussion with my Secretary of State I understand that you undertook to ascertain whether the formula the piece of paper sets out would be acceptable to the Chancellor.

Yours and.
Barr

C A Whitmore Esq

SECRET

PUBLIC EXPENDITURE REDUCTIONS

1. Pay and price increases in excess of the provision made in the Ministry of Defence's cash limit will cut the volume of defence expenditure next year (1980/81) below provision agreed by Ministers at survey prices. Defence spending will also be reduced if the cost of the Government's decisions on the recommendations of the Armed Forces Review Body exceeds the provision available within the cash limit, since the defence programme would have to be cut to make up the difference.

2. In recognition of these factors, and of the special position of defence, the Ministry of Defence's cash limit for 1980-81 will be:-

i. Raised as necessary to cover the cost of Government's decisions on the recommendations of the Armed Forces Review Body; and

ii. Kept under review with a view to ensuring that there is a real increase in defence expenditure in 1980/81 in line with the agreed NATO target of aiming for annual increases in real terms in the region of 3%.

for the and will otherwise the same as the cash limit agreed for other public expenditure programmes, but subject to the higher of (a) NATO commitments and (b) the international economic situation.

in the light of economic and international circumstances

as in the agreed NATO target.

3. As a contribution towards the measures necessary for a major reduction in public expenditure in 1980/81, the Defence Secretary will place a moratorium on major new works services of a non-operational character in order to achieve a reduction in defence spending of £50M in 1980/81. The planned defence figure of £8062M published in Cmd 7746 for 1980/81 will be reduced to £8012M at survey prices.

4. Decisions already taken on defence figures for 1981/82, 1982/83 and 1983/84 will remain unchanged.



29 JAN 1960





MINISTRY OF DEFENCE
MAIN BUILDING WHITEHALL LONDON SW1
Telephone 01-~~XXXXXX~~ 218 2111/3

MO 21/2/25

29 January 1980

Phnt

Dear David,

DEFENCE WHITE PAPER: NORTHERN IRELAND

On the agenda for Cabinet on Thursday is the Statement on the Defence Estimates 1980, a draft of which has already been circulated under cover of C(80)8. The Defence and Overseas Policy Committee did ask the Defence Secretary to review, in consultation with the Secretary of State for Northern Ireland, the section in the White Paper on Northern Ireland. I attach for your information the slightly modified text of paragraph 502 of the White Paper which my Secretary of State and the Northern Ireland Secretary are agreed would give a clearer picture of the aims of the Government's longer term policy.

I am sending copies of this letter to the Private Secretaries to the members of Cabinet and to the Private Secretaries to the Minister of Transport, Minister of State, Civil Service Department and the Parliamentary Secretary, Treasury.

Yours sincerely,

David Omand

(D B OMAND)

David Wright Esq
Cabinet Office

502. The Government's purpose is to restore normal life to the people of Northern Ireland. Removing the constant threat of violence is a first priority and vital to this is the work of the Services - demanding, often tedious and always dangerous. We look forward to a time when troops in Northern Ireland while remaining immediately available to assist the Civil power, can concentrate on training for their primary role in war. Already in many areas the Royal Ulster Constabulary can handle the bulk of the anti-terrorist task without military assistance. But in other areas a more active Army role remains essential. Much of their work in support of the RUC is necessarily spent on patrolling, whether in city streets or in open countryside, on checkpoints and on static guard and observations duties. But, since they are a prime target for terrorist attack, commanders take continual care that only necessary operations are undertaken. Great responsibility devolves upon junior NCOs and on individual soldiers. These duties, particularly searches of people and their vehicles, demand high levels of concentration, tact and sensitivity towards the community.

30 JAN 1960



Clive

Defence options

The figures are set out
on the last page of this note.
I have added the figures based
on 1976/80 ~~estimated~~ out-turn.

What the figures don't
show is the effect of a
cash limit squeeze in 1980/81.
But the Chancellor's proposed settlement
~~should~~ should give MOD some
real growth in that year.

R.

3

S E C R E T

DRAFT LETTER:

From: Mr M A Hall

To: Mr T Lankester, No. 10

DEFENCE EXPENDITURE

You told me that the Defence Secretary had asked to see the Prime Minister tomorrow in connection with the current discussion of the Defence Budget figures over the next four years. Such a meeting might in the Chancellor's view be helpful, since his own discussions with Mr Pym are - despite the Home Secretary's assistance - still deadlocked.

2. You may recall that the Chancellor proposed that for 1980-81 there should be a one-year moratorium on increases in defence expenditure, and that the Defence Budget should be set at the level of the latest 1979-80 forecast outturn. He offered 3% annual increases in the three later years of the Survey period. The Defence Secretary rejected this proposal, and offered in exchange a reduction of £50m on the Cmnd 7746 1980-81 figure. This offer was subject to two conditions, namely that the Defence cash limit for 1980-81 should be raised to accommodate the cost of the Government's decisions on the Armed Forces Pay Review Body's report, ^{that it} and should be kept under review to ensure that a real increase in defence expenditure in 1980-81 took place in line with the 3% NATO target. The Chancellor does not believe that it would be ^{right} ~~possible~~ to make a special exemption for Defence from whatever across-the-board decisions the Government takes on the cash limits regime for

S E C R E T

/1980-81

S E C R E T

1980-81, and the resultant volume squeeze. Nor did he regard the £50m conditional offer as an adequate MOD response to the requirement for a saving of £1bn next year ^{and £2bn thereafter.}

3. You may think that the Prime Minister should be aware of the outlines of a possible compromise settlement which has been worked out between officials ad referendum to Ministers. The main features are set out in the Annex to this letter. They would give the Defence Secretary much of what he has asked, and in particular:-

(a) a 3.6% increase in 1980-81 over the latest forecast of the 1979-80 Defence Budget outturn, with 3% annual increases thereafter. The 1980-81 figure is high enough to permit some real growth even if a 3% volume squeeze were imposed through the cash limit regime;

(b) ^a ~~the~~ concession on Armed Forces pay, to which he ^{in defence expenditure, and} apparently attaches importance; and

(c) figures for the last two years of the Survey period higher than those which were agreed in Cabinet in October, though lower than the totals of the Cabinet figures and the prospective Contingency Reserve claims which were discussed in the aftermath of Cabinet.

4. The Chancellor had hoped for a much larger contribution from the Ministry of Defence to the current reductions exercise: since it accounts for one-ninth of all Government expenditure, the Defence Budget, pro rata share of reduction, of £1bn and £2bn would be £110m and £220m. Nor is the Chancellor sure that Cabinet colleagues would allow Mr Pym to get off so lightly. But, if he could be sure that Mr Pym would accept the deal which has been worked out between officials, and

We understand
that Mr Pym
is unwilling to
accept it.

Flag A

S E C R E T

recommended by MOD officials, the Chancellor would be prepared to settle for it, and recommend it to Cabinet on Thursday. He would therefore be grateful if the Prime Minister could find an opportunity during tomorrow's meeting to urge Mr Pym to settle on the basis worked out by officials, and to warn him that to ask for still more concessions would mean that the substance of the matter would have to be debated in Cabinet on Thursday, where he might come under considerable pressure.

S E C R E T

DEFENCE EXPENDITURE

The proposal is that, for 1980/81:-

- a. the Ministry of Defence should not be exempt from whatever across-the-board decisions are taken on the cash limits regime and the resultant volume squeeze;
 - b. in recognition of the special position on Armed Forces Pay, the Treasury would however consider sympathetically any MOD proposal for an increase in the cash limits to accommodate the extra costs (above the 14% provision to be included at the outset) arising from the implementation of the government's decisions on the forthcoming Armed Forces Pay Review Board's recommendations;
 - c. as a contribution to the £1 billion reductions sought in 1980/81, the provision for the Defence Programme will be reduced from the Cmnd figure of £8062 million to £8000 million.
2. In 1981/82 to 1983/84:-
- a. the public expenditure White Paper will show a straight progression of 3% increases based on the 1980/81 figure of £8000 million; and
 - b. the Ministry of Defence will waive the prospective claims on the Contingency Reserve (for Polaris replacement costs) discussed in the autumn.

S E C R E T

3. These proposals are set out on line 7 of the attached table. Also shown are the savings (some £65 million p.a.) against the totals of the figures approved by Cabinet and the prospective Contingency Reserve claims; together with the very much smaller savings (negative in the last two years) which Cabinet colleagues would recognise.

Defence Programme

[Million at 1979 Survey Prices]

	1978/79	1979/80	1980/81	1981/81	1982/83	1983/84
1. July Cabinet Decision (announced in Cmnd 7746)	7509	7824	8062 (3%)	-	-	-
2. October Cabinet Decision (not announced)				8250 (2.3%)	8450 (24%)	8650 (2.4%)
3. Ceiling on Contingency Reserve Claims for Polaris Replacement Costs				54	103	160
4. Effective Later Years figures (2 + 3)				8304 (3%)	8553 (3%)	8810 (3%)
5. Treasury Proposed Reductions	7724	7724	7724 (-)	7960 (3%)	8200 (3%)	8440 (3%)
6. MOD counter-offer	7724	7724	8012 (3.75%)	?	?	?
7. Proposed settlement	7724	7724	8000 (3.6%)	8240 (3%)	8487 (3%)	8742 (3%)

8. Savings - i.e. line 7 compared with

a) cf lines 1 + 2	62	10	-37	-92
b) cf lines 1 + 4	62	64	66	68

3% growth based
on 1979/80 out-turn
(savings on lines 1 + 2)

7724	7956	8195	8441	8694
S E C R E T	106	55	9	-44

2/8 1980



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cc HO LPS
LCO DOT
FCO D/Ind
HMT NIO
LPO CO

10 DOWNING STREET

From the Private Secretary

28 January 1980

The Prime Minister has seen your letter to me of 25 January enclosing a new draft for the section of the Defence White Paper on Northern Ireland. She is content with this subject to the following two comments:-

a) Subject to the views of the Secretary of State for Northern Ireland she would prefer the first sentence to read "The Government's purpose is to restore normal life to the people of Northern Ireland":

b) She would prefer the third sentence to read "We look forward to a time when troops in Northern Ireland, while remaining immediately available to assist the Civil power, can concentrate on training for their primary role in war".

I am sending copies of this letter to the Private Secretaries to the members of OD, to Ian Ellison (Department of Industry), Roy Harrington (Northern Ireland Office) and David Wright (Cabinet Office).

M. O'D. B. ALEXANDER

David Omand, Esq.,
Ministry of Defence.

289



With the Compliments
of the
Chancellor of the Exchequer's
Private Secretary

Martin Hall

Treasury Chambers,
Parliament Street,
S.W.1.

SECRET



2

MINISTRY OF DEFENCE WHITEHALL LONDON SW1A 2HB

TELEPHONE 01-218 9000
DIRECT DIALING 01-218 2111/3

MO 8/2/12

28th January 1980

CHANCELLERY	
REC.	28 JAN 1980 sent 28/1
NAME	Mr. Hanford
COPIES TO	CST Sir D. Lias Sir A. Robinson Mr. F. E. A. Rostell

Dear Geoffrey,

DEFENCE EXPENDITURE Mr. Hanford

I fear I am not content to settle the 1980/81 problems on the basis suggested in your letter of 25th January. My reference to taking action to reduce the planned defence figure for 1980/81 by £50 m was subject to two conditions which you explicitly reject, namely that the defence cash limit for 1980/81 should be raised to cover the cost of the Government's decisions on the Armed Forces Review Body and should be kept under review with a view to ensuring that there is a real increase in defence expenditure in 1980/81 in line with the 3% NATO target.

I agree we must seek to settle the matter before Thursday; I am meantime setting out my views on the political implications of what you are asking of me.

John Major

Francis Pym

Francis Pym

The Rt Hon Sir Geoffrey Howe QC MP

SECRET



28 JAN 1960

Tim - herewith a letter
to Mr Ryan,
as provided.



2 PPS

M.

With the Compliments
of the
Chancellor of the Exchequer's
Private Secretary

Treasury Chambers,
Parliament Street,
S.W.1.

28/1



cc Ps/CST
 SIR O WASS
 SIR A RAWLINSON
 MR FER BURR
 MR KEAR
 MR HANSCROW

Treasury Chambers, Parliament Street, SW1P 3AG
 01-233 3000

21 January, 1980

Dr Francis

DEFENCE EXPENDITURE

Following our conversations earlier in the week, I have been reflecting on the points you put to me. I am sure that the time has come for us to settle the question of the 1980-81 Defence Budget.

I know the difficulties which tight cash limits impose on your budget, but the same is true of all cash limited programmes. It is clear to me that Defence cannot be exempt from whatever across-the-board decisions on next year's cash limits regime the Government takes. In particular, while I recognise your special concern about how the Government's decisions on the forthcoming Armed Forces Pay Review Board's recommendations might be funded, I do not see how we could envisage any special addition to your cash limits on this score. Even if the Board should recommend, and the Government agree, pay increases as much as 5 percentage points above the 14 per cent provision I have suggested should be included in your cash limits, the extra cost would represent only some 1 per cent of your budget, and its absorption should not present undue difficulty.

If you were prepared to accept these points, I would not press you further to increase the reduction of £50m you offered for 1980-81 and which you suggested should be subject to certain conditions. I hope that we can settle the 1980-81 problem on this basis, subject of course to Cabinet agreement, and I should be grateful if you could let me know on Monday whether you are content. If you are, we might instruct officials to consider as a matter of some urgency what figures would be appropriate for the three later years, since our colleagues will expect us to come to some conclusions about them too before Cabinet next week.

[Signature]
 (GEOFFREY HOWE)

The Rt. Hon. Francis Pym, MP



*After - but see covered
on final release. sub.*

MINISTRY OF DEFENCE
MAIN BUILDING WHITEHALL LONDON SW1
Telephone 01-930-7022 218 2111/3

MO 21/2/25

25 January 1980

(1)

Prime Minister

Dear Michael,

*Agree text? In Paper +
In Athens are content. 25/*

The OD meeting on 22 January concluded that the section of the Defence White Paper on Northern Ireland did not give a sufficiently clear picture of the aim of the Government's long term policy. My Secretary of State and SSNI were asked to produce a revision of that section of the Defence White Paper. This they have done and the attached revised paragraph would, in their view, meet the OD's requirement. Provided that the Prime Minister is content with this formulation, it will replace the existing paragraph 502 of the Defence White Paper as it has been circulated to Cabinet members.

I am copying this letter to the Private Secretaries to members of OD, to the Private Secretaries to the Secretaries of State for Industry, Northern Ireland and to Martin Vile in Sir Robert Armstrong's office.

*Yours sincerely,
David Omand*

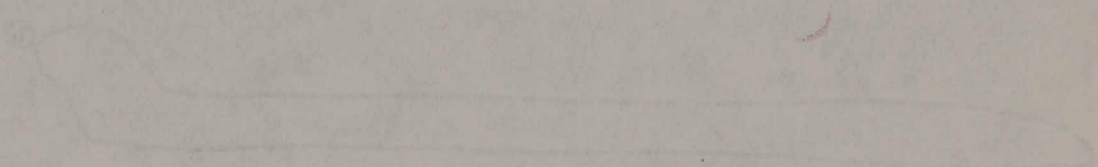
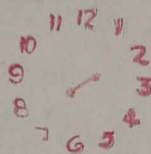
(D B OMAND)
Assistant Private Secretary

M O'D B Alexander Esq
No 10 Downing Street

502. The Government is determined to restore normal life to the people of Northern Ireland. Removing the constant threat of violence is a first priority and vital to this is the work of the Services - demanding, often tedious and always dangerous. We look forward to a time when troops in Northern Ireland can concentrate on training for their primary role in war, while remaining immediately available to assist the Civil power. Already in many areas the Royal Ulster Constabulary can handle the bulk of the anti-terrorist task without military assistance. But in other areas a more active Army role remains essential. Much of their work in support of the RUO is necessarily spent on patrolling, whether in city streets or in open countryside, on checkpoints and on static guard and observations duties. But, since they are a prime target for terrorist attack, commanders take continual care that only necessary operations are undertaken. Great responsibility devolves upon junior NCOs and on individual soldiers. These duties, particularly searches of people and their vehicles, demand high levels of concentration, tact and sensitivity towards the community.

- ① We have been determined to do this for some ten years without succeeding. Would it not be better to say The G's purpose is to restore order. Has the phrase been repeated many times?
- ② Would it not be better to change the order of this sentence as indicated.

25 JAN 1980



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PART 2. ends:-

C (80) 8.

PART 3. begins:-

MON to MA 25.1.80.

MO 21/2/25.

