

Ref: A01203

SECRET AND PERSONAL

PRIME MINISTER

Defence Expenditure

Prime Minister. 3

I understand that Mr Pyne has now asked for another work with the Home Secretary. They are hoping to meet tomorrow afternoon.

MT

SKW

22:30

As I told you, it was beginning to look as if we were heading for another confrontation between the Chancellor of the Exchequer and the Secretary of State for Defence on cuts in defence expenditure.

2. My information is that the Home Secretary has now persuaded the Secretary of State for Defence to consider seriously the possibility of offering cuts of £50 million a year for three years on non-operational expenditure - the building of officers' messes and so on.

3. The Secretary of State for Defence's price for this will be some softening of the Treasury attitude on his cash limits. He will want a "realistic" cash limit on armed forces pay (that is to say, one that ~~fully~~ enables him to accommodate the recommendations of the Armed Forces Review Body without any countervailing volume squeeze). He will also be looking for some relief on the cash limit of the rest of his expenditure. In terms of his civil servants he will clearly have to work to the same cash limit as the rest of Whitehall. It may, however, be possible to arrive at a separate cash limit for the rest of his expenditure, higher than that which is applicable to other Departments, by reference to some special factor still to be defined. My impression is that the Treasury would settle for that, in preference to any kind of arrangement which in effect let the Ministry of Defence off cash limits altogether.

RA

Robert Armstrong

22nd January 1980