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CONFIDENTIAL

MR. LANKESTER

R 617

Defence Cash Limit 1979-80

The Chief Secretary, Treasury has now commented on the minute of 2nd July from the Secretary of State for Defence. There are two points you might like to make in putting these papers to the Prime Minister:-

(a) On the immediate question of the Budget changes, the Chief Secretary took the Prime Minister's views on this in his minute of 4th June, and you said (your letter of 5th June to Alister Pirie) that she agreed 'that there should be no easement of the cash limit policy as already decided and announced on account of the higher RPI in the post-Budget forecast. She also agrees that Ministerial colleagues should be warned of the extra volume squeeze which this will imply ...'. Unless the Prime Minister is persuaded by Mr. Pym's latest minute that she should change her view on this, we assume that decision still stands. As the Chief Secretary will no doubt say, any special exemption from the existing cash limits for the Ministry of Defence would open up a whole series of similar claims. Equally, the Secretary of State for Defence has a strong case for special treatment, given that the Budget cuts wipe out much of the extra benefit he was given immediately after the Election, and the level of the Defence Budget has been frequently changed in the past, usually downwards, by the applications of considerations to which other spending programmes have not been subjected.

See Gen Pol (Pub Exp) Pt 2.

(b) But this case does not stand in isolation. The Secretary of State for Defence has also pleaded for special treatment for his Votes to take account of the cost of the impending pay increase for the industrial Civil Service (and 70 per cent of that falls on his Votes directly). No decision is needed on that point yet. For the moment, Treasury and CSD Ministers are assuming that the Cabinet's earlier decision,

to increase the cash limits would accommodate the settlement, but then to abate them by 3 per cent to take account of the extra cost of pay will stick. But it is relevant to the position of the Defence Budget that a number of our NATO allies e.g. West Germany may not regard the special treatment accorded to the Armed Services pay award as a true addition to the level of United Kingdom defence expenditure.

This is another illustration of the conflict of priorities between the Defence programme and the cash limit policy. And if it is not resolved in the way the Secretary of State for Defence wants, this issue might come to the Prime Minister's notice.

MJV

(M. J. Vile)

6th July, 1979