

SECRET



Defence

or Minister

SUBJECT

10 DOWNING STREET

From the Principal Private Secretary

13 November 1980

Dear Brian,

Defence Expenditure

The Secretary of State for Defence brought the Chiefs of Staff to see the Prime Minister yesterday afternoon so that they could let her know their views on defence expenditure.

The Chief of the Defence Staff said that he and his colleagues were grateful to the Prime Minister for agreeing to see them. They did not want to add to her burdens but they were very concerned about the country's declining military capability. Our operational capability was determined by the Soviet threat and by the Government's commitments. But the Chiefs of Staff thought that a dangerous divergence was developing between what was required and what could be provided with the resources available. OD had agreed in July on a re-shaped defence programme which would reduce our operational capability across a wide field. The decisions which Ministers had taken would reduce the base line of the defence programme, and at the same time the acquisition of Trident had to be accommodated within the money available, for this programme had not been previously allowed for within the defence programme. He had told OD at that time that the prudent limit of the defence programme had now been reached, and that had been on the assumption that an appropriate level of defence expenditure would be available. Since then the world had become a more dangerous place. Moreover, the defence programme had come up against the difficulties imposed by the cash limit. The Ministry of Defence had taken emergency measures to restrain its spending. There had been the moratorium on equipment contracts; all new works service had been stopped; recruitment to the forces had been reined back; and in order to save fuel there had been a 30% cut-back in activity and war reserves had been depleted. These steps were unprecedented since the War. It would, however, be possible to recover from them provided they were short term measures only. But if defence expenditure was to be cut in 1981/82 and similar measures became necessary, the programme could become unmanageable and it might not be possible eventually to recover. The Chiefs of Staff were worried that next year's cash limit would be too small and that whatever pay award the Services received would have to be accommodated within it.

/The CDS

SECRET



SECRET

- 2 -

The CDS continued that it was important to understand the long term nature of the defence programme. Expenditure was committed far in advance, and this left little flexibility in the early years. Nine-tenths of the defence budget for any particular year was committed at the outset of that year: in today's terms, this meant that roughly £1 billion was uncommitted, but half of that was needed for unavoidable expenditure on things like fuel and food. This was a measure of how difficult it would be to accommodate the cut in the base line for 1981/82 which the Treasury were seeking. Moreover, a cut of £188 million next year represented a reduction of £2 billion over the 10 year programme; this was the equivalent of half the cost of Trident or the cost of two major projects. It would require a fundamental re-shaping of the defence programme. The Services would not be able to meet their commitments with a capability which Chiefs of Staff judged to be sufficient. They would be facing the forces of the Warsaw Pact with inadequate equipment. The nuclear threshold, which was already low, would come down still further. If the proposed cuts were made the Government would have a choice between running a risk which, in the view of the Chiefs of Staff, would be dangerous and cutting the commitments which the Armed Forces now fulfilled.

The Chief of the Air Staff said that he could best exemplify the effect of present and proposed cuts on the RAF's capability by looking at the air defence of the United Kingdom. The Soviet air threat against the UK was estimated to be made up of 250 bombers or more. At the moment we could muster about 100 fighters in response. Last year the Government had decided on some interim improvements, including an additional Lightning Squadron and running on three Phantom Squadrons, until the Tornado ADV came into service. An annual increase in expenditure of 3% would allow these improvements to be made and the number of aircraft to be built up to the 150 which were assessed to be necessary to do the job. These plans had had to be trimmed back in the light of OD's decisions in July. Further cuts now would mean that the plans to form the Lightning Squadron would have to be dropped and the Shackleton Airborne Early Warning Squadron would have to be disbanded early leaving a three year gap in AEW cover until the introduction of the Nimrod. These measures, together with others, would leave the air defence of the UK in a worse state than it had been when the Government came into power. It was not possible to improve our capability in this field by transferring resources from elsewhere. The transport force, which was at half the level of five years ago, was now at the minimum required to meet its war role and to provide an out of area capability. The Nimrod surveillance force was at the lowest possible level at which an adequate check of Soviet activity in the Eastern Atlantic could be made, and our tactical air capability was already below its planned numbers. If further cuts in expenditure were made, we could be prejudicing the ability of the RAF's air crews to carry out the tasks laid upon them.

/The Chief of the Naval

SECRET



SECRET

- 3 -

The Chief of the Naval Staff said that even the measures to achieve the expenditure targets in the 1980 White Paper would cause severe damage to the present and future capability of the Fleet. Moreover, the naval programme would be cut by £1.3 billion as a result of OD's decisions in July. This meant that by the end of the next financial year planned orders for one nuclear submarine, four frigates, 15 mine sweepers and 30 aircraft would not be placed; and no major surface warship would be ordered in the first three years of this administration, something which was unprecedented in the recent past. The implications for the Navy's industrial base were very serious. It was possible that three shipyards would have to close, with the loss of 15,000 jobs in the ship building industry and three or four times that number in ancillary industries. There had already been a 30% cut in the Fleet's activity this year in order to save expenditure on fuel. All these steps meant that the Fleet's ability to do its job had already been severely reduced. If there were more cuts in 1981/82, the fighting efficiency of the Navy would be lowered still further. A cruiser, a destroyer and two frigates would have to be sold or scrapped, and one Royal Marine Commando disbanded. There would have to be further reductions in orders for new ships. Our force declarations to NATO would have to be revised; and this at a time when the Alliance was calling for an increased naval effort. The Soviet Union was building three new classes of nuclear submarines, with one submarine being completed every eight weeks, and four new classes of surface warship. In his professional judgement the cuts which the Navy were being forced to make would prejudice the adequate security of the United Kingdom for a long time.

The Chief of General Staff said that he had been trying to improve what he called the staying power of the Army. The role of BAOR, with our allies, was to win any war in Europe or if that were impossible, to create a breathing space in which Governments could take decisions about the use of nuclear weapons. In May 1979 our forces in Germany had been capable of intensive fighting for only 4-5 days. The aim had been to increase this period to 8-10 days. But, following OD's decisions in the summer, the core of the Army's equipment programme would have to be cut, and it would not be possible now to improve on the period of 4-5 days.

The CGS continued that he was also concerned about the quality of the Army's equipment. The growing sophistication of Soviet weapons could not be ignored, and we had to match it to an extent if we were to survive. Already there had been cuts - for example, in night vision equipment, our long-range target acquisition capability and in the Rapier programme - and if expenditure were reduced again, there would have to be further cuts which would mean that the Army simply did not have the equipment to do the job. Moreover, combat units would have to be disbanded, and it would be impossible to meet existing commitments, let alone any new ones. Training would have to be continued at the restricted level which had applied during the last few months. These measures would be seen by the Army as a volte-face in policy, and morale would inevitably be affected.

/The Secretary of State

SECRET



The Secretary of State for Defence said that an annual increase of 3% in real terms sounded good but it was actually a negative figure because real costs of equipment were growing all the time with increased sophistication. Nonetheless, in the light of the general economic situation, he had accepted a smaller increase in the cash limit for this year than was strictly required. He had now offered, in the present review of public expenditure, a reduction of £152 million in the planned defence budget for 1981/82, subject to certain conditions. As he had made clear to the Cabinet, the Chiefs of Staff did not recommend this reduction: on the contrary, they believed that the defence budget should not be reduced at all.

The Prime Minister said that she would like to spend as much as possible on defence, but the fact was that she could not ignore the overall economic state of the country. We were now in a very deep recession which was world-wide and OPEC-induced. Our allies were also affected, and a number of them were reviewing their own defence programmes. The FRG, which was in the front line, was expecting to increase its defence budget this year by only 1.7%. We were now facing a PSBR of between £11 and £13 billion next year. Financing a borrowing requirement of this size was bound to keep up interest rates, and this would place an enormous burden on industry. This was why it was essential to keep public expenditure totals to those published in the White Paper of March of last year. Even so, she accepted that in the judgement which Ministers had to make about where reductions in public expenditure should fall in order to accommodate excesses in other programmes, defence should continue to have some priority. Last year, defence expenditure had shown an increase of 3%. If the defence budget was overspent this year by £70 million - and although she did not wish to encourage overspending all the signs were that the defence excess would be over this sum - the increase would again be about 3%. This was better treatment than other programmes had received. Next year the defence budget would be of the order of £10 billion. She accepted that a reduction of £500 million or even £400 million was not attainable. But she believed that a reduction of £250 million should be possible. This was only £60 million more than the saving which would be produced by the application of the 2% volume cut to cash limited programmes which other Departments were accepting. A reduction of this size was very small in relation to the total size of the defence budget, particularly coming after two annual increases of 3 per cent. She did not believe that a cut of this order would materially affect the Soviet Union's assessment of the defence capability of the United Kingdom and, much less, of the capability of the Alliance as a whole. Even with a cut of £250 million, defence spending would still rise by 1.9%. She understood the desire of the Chiefs of Staff for a stable base-line on which to plan their programme, but she could not say what resources would be available over ten years, any more than the Chiefs of Staff could say where the forces would be deployed in 1990. The fact was that in today's economic circumstances no programme could be allowed to have its volume regardless

/of cost.



of cost. In any case, an approach of that kind would provide no incentive to efficiency. Firms in the private sector were cutting costs very hard and she believed that there was scope for similar action in defence establishments like the dockyards. She was, however, prepared to accept that the MOD should not have to find the entire Armed Forces pay increase due next April from within whatever cash limit was applied to the programme as a whole.

The CDS said that the Chiefs of Staff understood the international and national problems facing the Government, not least its economic difficulties. He acknowledged that the Government could spend on defence only what the country would bear. But the job of the Chiefs of Staff was to report to the Prime Minister what defence capability the available resources would provide. They believed that if the defence programme approved by OD in July was to be carried through, there should be no reduction at all in the levels of defence expenditure announced in the spring. This year's overspending was due to faster billing by industry than had ever been known before and to a cash limit which was unrealistically low in relation to inflation in the defence field. If next year's cash limit was also set too low and if the MOD had to absorb all or even part of the Forces pay increase, the programme would have to be reined back to avoid an overspend. In addition there was now the prospect of cuts in defence expenditure as part of the current review of public expenditure. A cut of £250million next year would be £2.5 billion over the 10 year defence programme, and this would mean projects and men would have to go. The tail had already been cut back over the last decade and efficiency generally was high: there was little scope for savings in this area. The decision on the allocation of resources was of course entirely a matter for Ministers. The Chiefs of Staff were simply saying that if planned defence expenditure had to be reduced, they wanted their commitments cut. They would then reshape the defence programme accordingly. Anything less was not fair on the Forces. Servicemen should not be asked to carry out commitments with inadequate resources. It was not for the Chiefs of Staff to recommend which commitments should be given up: that was for the FCO, but they would be ready of course to give their professional military advice in any review of commitments. But the Chiefs of Staff had to warn Ministers that any move in this direction would have serious implications for the cohesion of the Alliance. The United States were calling for a bigger increase in defence spending than 3% per annum and wanted their European allies to do more outside the NATO area. The Europeans were unlikely to agree to this. If the UK, which had hitherto been giving a lead to the Alliance in improving its defence effort, then reduced its commitments, the United States might well decide to do less in Europe. This could lead to decoupling and eventually to the disintegration of NATO.

The CAS said that the planned budget for the RAF for 1981/82 had originally been £2954 million. Following OD's decisions this had been reduced to £2878 million. When committed expenditure on things like pay and pensions was allowed for, there was less than £200 million to play with. It was, of course, possible to cancel existing contracts, but any savings would be offset by the payment of cancellation charges.

/The CGS said



SECRET

- 6 -

The CGS said that to argue that a defence budget of £10 billion should have no difficulty in finding economies of only £60 million was to overlook two important points. First, as the CDS had made clear, the savings in one year would be extended over future years, so that what appeared to be a small cut was in fact a major reduction in the defence programme. Second, savings in the short term had to be found from the relatively small sums of uncommitted money and this inevitably meant that measures had to be taken which made little sense when seen against a longer time-scale and which could severely damage the Forces' capability. It should be borne in mind that the Chiefs of Staff had said that they would give Trident high priority within the defence programme on the basis that our conventional capability would not be affected as a result. But cuts of the size now under discussion would undoubtedly affect the conventional capability.

The CDS thanked the Prime Minister for giving him and his colleagues the opportunity to set out their views so fully. He repeated that their advice had to be that there should be no further reductions in planned defence expenditure. But if Ministers decided that there should be such cuts, the Chiefs of Staff felt that there should be a corresponding reduction in commitments. They had found the discussion with the Prime Minister very valuable and they hoped that she would be ready to see them informally from time to time.

The Prime Minister said that she was grateful for the advice of the Chiefs of Staff. She would consider it further in the context of the wider economic situation of the country. She would be very ready to meet the Chiefs of Staff in future, as the CDS had proposed.

I should be grateful if this letter could be circulated within the Ministry of Defence only to those who have a strict need to see it. I am sending copies of it only to John Halliday (Home Office), George Walden (FCO), John Wiggins (Treasury) and David Wright (Cabinet Office), and they too should similarly restrict its further circulation.

Yours ever,

Alvin White.

B.M. Norbury, Esq.,  
Ministry of Defence.

SECRET

MEM