



MINISTRY OF DEFENCE
MAIN BUILDING WHITEHALL LONDON SW1
Telephone 01-~~9307682~~ 218 2111/3

MO 8/2/12

30th December 1980

*Jew Clive,*DEFENCE ESTIMATES 1981/82

You have suggested that it would be helpful in advance of the meeting arranged for tomorrow if we were to set out in more detail the steps leading up to my Secretary of State's decisions on the Defence Estimates set out in his minute of 23rd December to the Prime Minister.

The problem we face is the scale of the total reduction needed and the short timescale in which measures must bite if they are to produce savings early enough in the Financial Year, the start of which is now only 3 months away. Only a small proportion of planned expenditure for next year remains uncommitted and reductions in this area must be correspondingly large. Furthermore, some measures which will save money in the long term can cost more in the short term, for example because of redundancy payments or the need to provide works services before bringing about redeployments.

One of the purposes of our annual Long Term Costings is to bring our physical programme assumptions (eg planned deployments and front-line strengths) into line with our financial allocations. It is our normal experience that when as part of this process Estimates are prepared each year the total cost of the programme is higher than the target to which we are working. This is brought about by the overall effect of a myriad of changes in the programme and by the annual recosting of projects, particularly those in development, which tend to show cost growth as we get closer to the spending year. In the process of screening Estimates such excesses are eliminated by pruning back individual projects, by removing items/ or deferring/and by taking account of the benefits from planned increases in efficiency, redeployments and so forth.

C A Whitmore Esq



We have done this this year but it has been more difficult than usual. This is partly because some of our room for manoeuvre has been pre-empted by the programme adjustments which have had to flow from the decisions of OD in July (based on a higher defence budget). It is also partly due to the very large number of measures taken to restrain cash spending this year, including the three-month moratorium. Although we have done our best to try and find savings measures this year, such as reduced fuel consumption, of a once-off kind, inevitably a good deal of what we have had to do has had the effect of pushing expenditure out of this year into next.

On top of this normal process we are having to cope with the unprecedented shift in assumptions about short-fall in industrial production, which as Mr Pym has said has meant finding £360m of compensating reductions elsewhere in the programme to balance the increased industrial expenditure on existing projects, and finally the volume reduction of £200m imposed by Cabinet. The Service Boards (under the Chairmanship of the Service Parliamentary Under Secretaries) and the Central Staffs under the direction of the Secretary of State have combed through every area of the programme to find the least damaging ways of making these cuts. Annex A to Mr Pym's minute set out the major measures in terms of military, political and industrial impact. Although this highlights equipment and front-line measures, it also includes substantial savings in, for example, works services (£92m), fuel stocks (£50m), and recruitment (£12m).

There is in addition a very long list of minor items where decisions have been taken to reduce expenditure, particularly in the support area, as the following examples which I have drawn at random show:-

- a. complete cancellation of the buy of binoculars for the Army next year.
- b. cuts on clothing purchases
- c. reductions in duty travel for both servicemen and civilians
- d. deferment of essential orders for locomotives for the Army (used for outloading ammunition)



- e. 20% cut in all purchases by schools and colleges
- f. reduced level of window cleaning in the Army
- g. 10% cut in Army expenditure on postage, maps etc
- h. 22½% cut in HM Ships and RFA fuel consumption
- i. 25% cut in Army non-NATO exercises
- j. reduced medical stores stocks

Moreover the vigorous search for economy in the support area, such as the R&D Establishments, continues. But it would be unwise to count confidently on securing new significant savings as soon as next year. It takes time, even after decisions in principle are reached, to consult and then to redeploy people and dispose of property.

To re-iterate the point I made at the start of this letter the room for manoeuvre in the short term is very limited. About 40% of the defence budget goes on civil and military pay and service pensions. We have a very creditable record on civilian reductions and face a daunting task in meeting the latest forward targets set by the Lord President. My Secretary of State does not believe we can go further and still meet the requirements of the programme. On service personnel, we are already planning on making savings by cutting back on recruitment.

A further 40% of the budget is spent on equipment. Much of this is already committed (typically about 90% of planned expenditure on major equipment is committed before the start of the Estimates year). This does not mean there is no scope for change (apart from cancellation): we are for example studying urgently the possibility of devising a system of cash rationing of firms for existing projects, but again we cannot count with confidence on savings here yet. Mr Pym has also been examining whether it would be possible to respond to Germany's financial worries about Tornado (on which we shall be spending nearly £700m next year) and slow the programme down, but present advice is that this would not lead to cash savings next year. Because of the contractual and industrial difficulty of reining back on projects which are well ahead, we have no alternative but to look to projects in their early stages. Because they are spending relatively little



individually, a large number have had to be cancelled or deferred. We have also had to bear in mind that reductions have also been agreed in defence budget targets in later years, and we need therefore to remove now some items scheduled to be heavy spenders later on.

There are other judgements underlying the choice of measures. Deferments of equipment may be preferable to cancellation, and bringing forward the planned phasing-out of some units (particularly the older warships) may be preferable to cutting even further into equipment in production. The RN, for example, have 2 ASW carriers, 4 nuclear submarines, 7 destroyers, 4 frigates and 8 MCMVs on order and major weapon systems such as Sub-Harpoon and Stingray. 2 Type 42 destroyers, a Type 22 frigate, 2 MCMV, 2 OPV, a new sonar and the Mk 24 Torpedo are expected into service next year. The Army have given priority to their major items such as Challenger, Ptarmigan, Clansman, Rapier, Milan and Blowpipe now on order. The RAF plans to spend £675m next year on the two types of Tornado aircraft (strike/attack and air defence), £70m on the Nimrod airborne early warning aircraft, substantial sums on the Harrier (including the improved version) and the Jaguar, and major weapons projects such as an airfield attack weapon and various air-to-air missiles, existing and projected.

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

Yours crew,

David Omand

(D B OMAND)