

Defence Budget.

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PRIME MINISTER

cc Mr. Gifford
Mr. Haskins
Mr. Walters
[Signature]

You can discuss this at the meeting with Mr. Nott on Monday, which the Chancellor and Sir Keith are also attending. The few outstanding issues seem to be x and y below. I am told that the Chancellor is now prepared to go along with an early flotation.

BAe FLOTATION

Play A

I have now had a chance to study the issues which arise from Norman Tebbit's minute to you of 7th January.

x || 2. The first question is whether we can make public in time the £200M reductions in previously planned defence expenditure for 82/83 and 83/84 which are not at present due to be disclosed until the publication of the Public Expenditure White Paper in early March. As you know I shall be discussing with you on Monday an early general statement about next year's defence programme. This might be drafted in terms which meet this point.

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3. More difficult are the problems related to the defence workload for British Aerospace. We are able, of course, to point to our clear indication to resume 3% real growth in defence spending after next year; and we can point to a clear and distinct share of the defence budget which British Aerospace have secured in the past. But I cannot be specific now about exactly how much money they will get from us over the next few years nor about which projects they will have - nor, of course, could I for any other firm.

y || 4. I recognise the great political importance of flotation for our objectives as a Government, and its importance for a thriving aerospace sector. I am concerned, however, that the conditions for a flotation now could create difficulties for me in conducting the sort of fundamental look at defence commitments, roles, and capabilities which even a few days in office has convinced me is necessary.



5. I have been able to rephrase for the present the Sea Eagle project - a key programme I am advised for proceeding with flotation - and research and development on this will continue for the time being. I am going to negotiate with British Aerospace on the basis of a plan we have developed with them for containing future levels of expenditure in any one year, and their initiating now a review of the structure of the Dynamics Group (involving the closure of a major site) to be effected in about 5 years time. Even so, I cannot exclude the possibility that, when I come to my review of the forward programme, cancellations and adjustments affecting British Aerospace, not, excluding Sea Eagle, may be necessary. If flotation proceeds, therefore, it must be on the understanding that my freedom to act is not constrained. Whether flotation can legitimately proceed on that understanding must be open to some doubt.

6. I do not know whether flotation in May would be any easier than flotation now. But given what I have said above, which must be disclosed to Kleinworts and British Aerospace, the prospectus will need to be drawn up in terms consistent with the wider objectives I have described.

7. I am copying this minute to the other members of E and to Sir Robert Armstrong.

16th January 1981
Ministry of Defence