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/ March 1982

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Prime Minister.

*The Chancellor is not disagreeing with the MISC 7 decision to go for D5 but is putting down a marker on costs.*

*New Idm,*

*PM*  
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TRIDENT

The Chancellor has seen with interest Robert Wade-Gery's minute to you of 28 February, and is grateful for so prompt a report on the outcome of last week's talks in Washington.

The (public) American statement on offset is new, and to be welcomed. But it does not in itself bring any concrete benefit to the UK: it may not be easy to convert the words into actual contracts for UK firms; and such contracts would not of course be of direct benefit to the Defence Budget.

The Chancellor's main comments are on the cost of the D5 missile system. He is glad to see that the facilities charge has been waived. Annex E to Robert Wade-Gery's minute shows an improvement in the total levies package under the new deal of some \$35m over the 1980 agreement. But the Chancellor's impression is that, taking account of the extra \$65m or so which the UK now expects to bear for the Rapier defence of USAF forces here, the UK will still be paying some \$30m more than would have been incurred under the 1980 agreement.

Secondly, the costs of the C4 missile were much better established in 1980 than are the costs of D5 now. Under the present terms, the Defence Budget has no protection against real escalation in D5 costs; nor has any fixed schedule of payments yet been agreed. The Chancellor understands that the latest American computer run shows a raw figure for D5 costs falling to us some £330m higher than the figures on which the MISC 7 paper, the draft Defence Open Government Document, and the negotiations have been based. He is also aware that the Americans argue that this raw figure needs some adjustment, and that it is probably too high. Nevertheless, it is disturbing that such hints of substantial (10 per cent) real cost escalation should appear so early in the programme. (While it is good that the R & D levy is fixed regardless of real escalation, every £330m increased in the total costs would of course add \$10m to the overheads charge).

/In sum,



In sum, the Chancellor's view is that the deal now negotiated is probably the best we could have got without direct dealings between Heads of State, and that it is doubtful whether it could be improved in such dealings. It is tolerable, and no doubt presentable to the House and the public. But it has no bearing on the major part of the programme (the work to be done in the UK on designing and producing the submarine and the warhead) on which substantial cost escalation must be expected. The likely overall cost of the Trident project still causes him considerable concern.

I am copying this letter to those who received copies of Robert Wade-Gery's minute.

*Yours ever,*

*J O Kerr*

J O KERR  
Principal Private Secretary



CONGRESS

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