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AMENDED DISTRIBUTION & SEPTEMBER 1981

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FM WASHINGTON 012246Z SEP 81

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TELEGRAM NUMBER 2565 OF 1 SEPTEMBER

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PRESIDENT REAGAN AND THE ECONOMY

1. PRESIDENT REAGAN WAS RIDING HIGH WHEN HE LEFT WASHINGTON FOR A CALIFORNIA HOLIDAY A MONTH AGO. AS HE RETURNS TO WASHINGTON THIS WEEK IT IS BECOMING INCREASINGLY RECOGNISED THAT HIS TACTICAL VICTORY IN SWEEPING HIS BUDGET AND TAX CUT LEGISLATION THROUGH CONGRESS TEMPORARILY MASKED THE UNDERLYING ECONOMIC PROBLEMS WITH WHICH THE ADMINISTRATION MUST NOW GRAPPLE.

2. THE ADMINISTRATION ARE COMMITTED TO CONTINUING THE FIGHT AGAINST INFLATION AND VOLCKER (CHAIRMAN OF THE FEDERAL RESERVE BOARD) HAS PUBLICLY DEFENDED THE FED'S COMMITMENT TO FIGHTING INFLATION BY A REDUCTION IN THE GROWTH OF MONEY AND CREDIT DESPITE A STATEMENT BY REAGAN LAST WEEK THAT HIGH INTEREST RATES WERE QUOTE HURTING US IN WHAT WE'RE TRYING TO DO AS MUCH AS THEY'RE HURTING ANYONE UNQUOTE. IF THE ADMINISTRATION'S POSTURE IS TO CARRY CONVICTION (AND THEY'RE RELYING HEAVILY ON CREATING THE RIGHT EXPECTATIONS) THEY HAVE TO FIND A WAY OF MEETING THEIR COMMITMENT TO BALANCE THE BUDGET BY FY 1984 AT A TIME WHEN THE DEFICIT, FUELLED BY LOW GROWTH AND SLOWLY RISING UNEMPLOYMENT, MAY BE DOLLARS 20 BILLION OR MORE OVER THE CURRENT ESTIMATE OF DOLLARS 42.5 BILLION FOR FY 1982. THE ADMINISTRATION ARE COMMITTED TO FINDING A FURTHER DOLLARS 30 BILLION IN BUDGET SAVINGS FOR FY 1983 AND DOLLARS 44 BILLION FOR FY 1984. SINCE THE BUDGET FOR FY 1983 MUST BE PRESENTED TO CONGRESS IN JANUARY OF NEXT YEAR, THE INESCAPABLE CONCLUSION IS THAT FURTHER DRASTIC BUDGET CUTS MUST BE FOUND IN THE VERY NEAR FUTURE. OTHERWISE ANY RETURN OF BUSINESS CONFIDENCE GENERATED BY THE TAX CUT MAY BE LARGELY OFFSET BY THE HIGH LEVEL OF INTEREST RATES AND FEARS OF THE CONSEQUENCES OF A GROWING BUDGET DEFECIT.

3. THE IMPACT OF THE PUBLIC SPENDING CUTS ALREADY MADE BY THE ADMINISTRATION HAS YET TO BE FELT SINCE THEY HAVE NOT AS YET TAKEN EFFECT. BUT THE CUTS WERE SWINGING, EG THE ELIMINATION OF THE DOLLARS 122 MINIMUM MONTHLY PAYMENT TO ALL NEW RECIPIENTS OF SOCIAL SECURITY; AXING 300,000 PUBLIC SERVICE JOBS UNDER THE CETA PROGRAMME; REDUCING MEDICAL AID BY ABOUT 1 BILLION A YEAR AND TAKING AT LEAST 1 MILLION PEOPLE OFF THE FOOD-STAMP PROGRAMME. IT WILL BE DIFFICULT TO TRIM MAJOR CIVIL PROGRAMMES SUCH AS SOCIAL SECURITY FURTHER WITHOUT CREATING A CONTROVERSY WHICH WILL STRAIN CONGRESSIONAL LOYALTY TO THE PRESIDENT EVEN FROM CONGRESSMEN REPRESENTING REPUBLICAN DISTRICTS, SINCE THIS WOULD AFFECT NOT ONLY THE POOR

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AND DISADVANTAGED BUT THE GENERAL POPULATION AS WELL. NOR WILL IT BE EASY TO TRANSFER FURTHER EXPENDITURE POSSIBILITIES TO THE INDIVIDUAL STATES; STATE GOVERNORS ARE ALREADY SMARTING FROM THE REDUCTION IN FEDERAL AID WHICH THEY HAVE RECEIVED UNDER THE CUTS ALREADY PASSED BY CONGRESS, AND WILL NOT READILY AGREE TO FURTHER REDUCTIONS.

4. PRESIDENT REAGAN HAS ALREADY BROKEN HIS HOLIDAY TO HAVE MEETINGS WITH WEINBERGER, STOCKMAN AND MEESE TO TAKE A PRELIMINARY LOOK AT WHERE CUTS MIGHT BE MADE IN THE DEFENCE BUDGET WHICH HAD BEEN DUS TO RISE BY 7 PER CENT PER ANNUM FROM DOLLARS 180 BILLION IN FY 1981 TO DOLLARS 333 BILLION IN FY 1985. ALREADY MEESE HAS BEEN QUOTED AS SAYING THAT THE 7 PER CENT GROWTH FIGURE WAS A ROUGH TARGET FOR PLANNING PURPOSES, NEVER AN ABSOLUTE FIGURE. WEIDENBAUM (CHAIRMAN OF THE COUNCIL OF ECONOMIC ADVISERS) SAID IN A TELEVISION INTERVIEW AT THE WEEKEND THAT CURRENT PROPOSED DEFENCE SPENDING INCREASES WERE QUOTE EXTREMELY GENEROUS UNQUOTE; LESS RAPID EXPANSION MIGHT BE IN ORDER. HE WENT ON TO SUGGEST CHANGES IN THE YARDSTICK USED FOR INDEXING SOCIAL SECURITY BENEFITS IE MOVING AWAY FROM THE CONSUMER PRICE INDEX TO SOME OTHER INDEX LESS DISTORTED BY FACTORS SUCH AS THE COST OF HOME OWNERSHIP.

5. WHILE THERE IS NO DOUBT, THEREFORE, THAT THE ADMINISTRATION WILL AGAIN COMB THROUGH ALL OTHER PROGRAMMES FOR POSSIBLE SAVINGS, IT IS INCREASINGLY CLEAR THAT THEY HAVE NOW REACHED THE POINT WHERE TO ACHIEVE THEIR OBJECTIVES THEY WILL HAVE TO LOOK HARDER AT THE DEFENCE PROGRAMME AND THE SOCIAL SECURITY SYSTEM. CUTS IN THE PROJECTED GROWTH OF DEFENCE SPENDING MAY BE MORE PALATABLE POLITICALLY THAN MAJOR CHANGES IN THE SOCIAL SECURITY SYSTEM (WHICH WOULD BE ATTACKED BY THE DEMOCRATS AS AN ASSAULT ON AN ENTITLEMENT FOR WHICH AMERICANS HAVE PAID). BUT IT WILL NOT BE EASY FOR AN ADMINISTRATION COMMITTED TO MASSIVE INCREASES IN DEFENCE SPENDING TO BACK OFF AFTER LESS THAN A YEAR IN OFFICE.

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