


CONFIDENTIAL [CULL]

FM WASHINGTON 290110Z MAR 82

TO ROUTINE FCO

TELEGRAM NO 1013 OF 28 MARCH

INFO SAVING PARIS, BONN, UKREP BRUSSELS, TOKYO, OTTAWA,
CONSUL GENERALS IN USAPRESIDENT REAGAN, CONGRESS AND THE ECONOMY 

1. THE REPUBLICAN LEADERS IN THE HOUSE AND THE SENATE HAVE PUBLICLY WARNED THE PRESIDENT THAT TIME IS RUNNING OUT FOR A BUDGET COMPROMISE AND THAT, UNLESS THE WHITE HOUSE IS PREPARED TO START NEGOTIATING BEFORE THE EASTER RECESS (WHICH STARTS ON 2 APRIL) CONGRESS MAY GO AHEAD AND TRY TO DRAW UP A BI-PARTISAN BUDGET OF ITS OWN.

2. THE PRESIDENT'S OPPOSITION TO ANY CHANGES IN HIS PROPOSED BUDGET HAS HITHERTO SEEMED TO BE SET IN CONCRETE, BUT MR REAGAN IS NOW UNDER PRESSURE NOT ONLY FROM HIS OWN PARTY IN CONGRESS, BUT ALSO FROM INDUSTRIALISTS, MEMBERS OF HIS CABINET AND FROM HIS OWN STAFF TO SUPPORT A COMPROMISE. LAST YEAR, FACED WITH CONGRESSIONAL DIFFICULTIES, THE PRESIDENT APPEALED DIRECTLY TO THE NATION FOR SUPPORT AND RECEIVED AN OVERWHELMING RESPONSE. THIS YEAR, THINGS LOOK DIFFERENT. THE PRESIDENT CANNOT COUNT ON THE UNQUALIFIED SUPPORT OF HIS OWN PARTY OR OF CONSERVATIVE DEMOCRATS. THE PUBLIC, TO JUDGE FROM THE OPINION POLLS, ARE NOW ALSO ANXIOUS THAT CHANGES SHOULD BE MADE. FOR THE FIRST TIME, THE POLLS SHOW MAJORITY SUPPORT FOR A CUTBACK IN PROJECTED DEFENCE SPENDING.

3. THE ELEMENTS OF A COMPROMISE MOST LIKELY TO HAVE A CHANCE OF ENACTMENT INCLUDE

(A) HIGHER TAXES THAN ORIGINALLY PROPOSED BY THE PRESIDENT, PERHAPS INCLUDING CHANGES IN THE TIMING OR AMOUNT OF THE 10 PER CENT CUT IN INDIVIDUAL INCOME TAX RATES SCHEDULED TO TAKE PLACE ON 1 JULY 1983:

(B) A SMALLER INCREASE IN DEFENCE SPENDING THAN THE PRESIDENT ORIGINALLY PROPOSED; AND

(C) A LIMIT ON THE AUTOMATIC ANNUAL ADJUSTMENT IN ENTITLEMENT PROGRAMMES, INCLUDING SOCIAL SECURITY.

4. THE PRESIDENT AND THE DEMOCRATS HAVE BEEN PLAYING A CAT-AND-MOUSE GAME. THE PRESIDENT WOULD LIKE TO PUT THE ONUS FOR CHANGING THE BUDGET ON THE DEMOCRATIC LEADERSHIP IN THE HOUSE OF REPRESENTATIVES THEREBY MAKING THEM RESPONSIBLE FOR UNPALATABLE PROPOSALS (HIGHER TAXES) AND AVOIDING A PAINFULLY PUBLIC DEMONSTRATION THAT HIS BUDGET DOES NOT HAVE THE SUPPORT OF HIS OWN PARTY IN THE SENATE, WHERE THE REPUBLICANS ARE IN THE MAJORITY. SPEAKER O'NEILL HAS SAID THAT HE IS WILLING TO DISCUSS A COMPROMISE BUT IS DETERMINED THAT THE PRESIDENT SHOULD CARRY AT LEAST EQUAL RESPONSIBILITY FOR WHATEVER CHANGES EMERGE.

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5. IF THE OUTLINE OF A COMPROMISE DOES NOT EMERGE BEFORE EASTER, THE ADMINISTRATION WILL HAVE ITS ARM EVEN MORE FIRMLY TWISTED IN MAY OR JUNE WHEN IT HAS TO SEEK AN INCREASE IN THE PUBLIC DEBT CEILING. IT IS AT THAT POINT THAT CONGRESS WILL HAVE MAXIMUM LEVERAGE ON THE ADMINISTRATION TO PROPOSE ITS OWN PROPOSALS.

6. CONGRESS FURTHERMORE HAS YET TO ADOPT A BUDGET RESOLUTION INCORPORATING THE SECOND ROUND OF BUDGET CUTS IN FY1982. GOVERNMENT SPENDING IS BEING MAINTAINED ON THE BASIS OF A CONTINUING RESOLUTION WHICH EXPIRES AT THE END OF MARCH. SPENDING AUTHORITY WILL THEREFORE HAVE TO BE RENEWED BY CONGRESS IF THE FEDERAL GOVERNMENT IS TO BE FINANCED BEYOND THE END OF THIS MONTH. THE HOUSE OF REPRESENTATIVES HAS PASSED A RESOLUTION EXTENDING SPENDING AUTHORITY UNTIL THE END OF SEPTEMBER. BUT A SIMILAR STOP-GAP MEASURE MAY RUN INTO DIFFICULTIES IN THE SENATE WHERE SOME REPUBLICANS ARE CONSIDERING CONTROVERSIAL AMENDMENTS DESIGNED TO USE BUDGET AUTHORISATION TO PURSUE SOCIAL GOALS EG TO LIMIT THE BUSING OF PUPILS TO STATE SCHOOLS.

7. IN SHORT, THE PRESIDENT AND CONGRESS ARE AT LOGGERHEADS AND THE BUDGETARY PROCESS IS AT A STANDSTILL. THE ADMINISTRATION HAS BEGUN BELATEDLY TO REALISE THAT A FAILURE TO TAKE ACTION SOON TO TRY TO BREAK THE DEADLOCK IS UNLIKELY TO WORK TO ITS ADVANTAGE. THE MAIN BLOCKAGE HAS BEEN THE PRESIDENT'S OWN RESISTANCE TO INCREASING INDIRECT TAXES, OR TAMPERING WITH THE DIRECT TAX CUTS WHICH ARE AN INTEGRAL PART OF HIS PROGRAMME. THE FIRST SIGNS OF GIVE HAVE NOW APPEARED IN THE ADMINISTRATION'S POSITION. THE WHITE HOUSE CHIEF OF STAFF, BAKER, HAS BEEN AUTHORIZED TO HOLD PRELIMINARY TALKS WITH THE DEMOCRATS ON WHERE THEY WOULD LIKE TO SEE CHANGES MADE. MEESE ACKNOWLEDGED YESTERDAY THAT CHANGES WOULD BE NECESSARY BECAUSE OF THE GROWTH IN ESTIMATES OF THE PROBABLE DEFICIT; THE ADMINISTRATION WOULD BE LOOKING FOR QUOTE AREAS OF AGREEMENT UNQUOTE WITH CONGRESS.

FCO PASS SAVING PARIS, BONN, UKREP BRUSSELS, TOKYO, OTTAWA

HENDERSON

FINANCIAL
NAD

[REPEATED AS REQUESTED]

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THIS TELEGRAM
WAS NOT
ADVANCED