

Prime Minister

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Treasury Chambers, Parliament Street, SW1P 3AG  
01-233 3000

A cri de coeur (which  
might have been addressed  
to Mr Nott).

PLS 6/7

PRIME MINISTER

PUBLIC EXPENDITURE AND THE DEFENCE PROGRAMME

I am concerned about the Parliamentary and public impact of what has been said recently about the consequences of the Falklands operation for defence expenditure.

2. The limited arrangements which we agreed a fortnight ago, and which were succinctly set out in your Private Secretary's letter of 22 June, may I fear be in danger of misinterpretation.

3. There is a danger that a climate of opinion is being created, not least amongst our own backbenchers, which believes that our defence programme has been jeopardised by lack of money and that substantial increases in defence expenditure, going well beyond 3 per cent annual real growth plus additional Falklands costs, are now to be expected.

4. It needs to be said that our record to date is good. We have accorded the highest priority to defence, standing by the NATO 3 per cent growth target even during a period of declining GDP - in contrast with our European allies. In real terms we are spending £500 million more on conventional naval forces than when we came into office. If we are not gaining the credit we deserve, it is only because we are not getting this message across.

5. Over-ambitious expectations, if allowed to continue unchecked, could damage our economic policies. I have little doubt that other colleagues will follow suit and publicly press claims for their own particular programmes. We shall be faced with strong pressure for





substantial increases in public expenditure which cannot be removed in the normal course of the public expenditure Survey. Our aim of holding public expenditure to its planned levels might be prejudiced, and such headroom as I had hoped to provide for tax reductions in the next Budget would then be threatened.

6. We cannot afford to allow the defence programme to pre-empt an ever-growing proportion of public expenditure. In the plans published in this year's Public Expenditure White Paper, defence accounted for 12.2 per cent of the planning total. Some increase in this proportion will be inevitable after Falklands additions. But to accommodate the defence bids made so far in this year's Survey, defence's proportion of public expenditure would have to increase by 20 per cent in three years. The implications for other programmes would be dire.

7. The usual response to this not unfamiliar dilemma would be to set up a major package of expenditure cuts and other economies. This could lead to an arbitrary amalgam of hastily thought-out short-term measures, the effect of which would be to impede economic recovery and possibly to damage the credibility of the Government. If, as is likely, some proved impracticable or unacceptable, further increases in public expenditure (and thus in borrowing or taxation) would be inevitable.

8. This might be avoided by greater circumspection in our current public statements. It is enough to promise that the costs of the Falklands operation will not prejudice our commitment to 3 per cent annual real growth. That alone will put a strain on our resources, which may require adjustment of other programmes. We should not encourage the belief that, on top of this, there will be major improvements in our defence capabilities which would require a still higher growth rate in defence expenditure, of proportions which would not be matched by any of our European NATO partners and which



we simply cannot afford. We should concentrate instead on more positive presentation of our real achievements in defence spending and capabilities.

*gh*

G.H.

6 July 1982



file BK  
Defence

8 July 1982

PUBLIC EXPENDITURE AND  
THE DEFENCE PROGRAMME

The Prime Minister was grateful for the Chancellor's minute of 6 July about the public impact of what has been said recently about the consequences of the Falklands operation for defence expenditure.

The Prime Minister has read this minute and noted it without comment.

John Kerr, Esq.,  
HM Treasury

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