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4th November 1983

See Willie

MINISTERIAL GROUP ON PUBLIC EXPENDITURE (MISC 99): DEFENCE PROGRAMME

Thank you for your letter of 3rd November setting out MISC 99's thinking about the Defence Programme.

I confirm that I have accepted the proposed manpower target of 170,000 at 1 April 1988 on the understanding set out in your letter.

The question of 3% real growth in 1986/87 is, as you know, to be dealt with separately.

As to the remaining issues, I am prepared to forgo my bid for increases to cover the extra cost of the 1983 Pay Review Body awards. We have dealt with the remaining questions of my bid for inflation compensation and the proposed figures for 1984/85 and 1985/86 as a linked package. I confirm that I am prepared to accept the figures of £17010M for 1984/85 and £18040M for 1985/86 (both including provision for the costs of our Falklands commitment) on the understanding that the publication of these figures will be accompanied by the following formulation which was agreed by myself and Peter Rees at your meeting this morning:

The Rt Hon Viscount Whitelaw CH MC



"Alone of its public expenditure programmes, the Government's defence policy is currently expressed in both volume and cash terms. In order to fulfil the Government's commitments up to and including 1985/86, the cash provision will be reconciled year by year in the light of the volume requirement and of the most up to date forecasts of inflation and appropriate adjustments made."

I am sending copies of this letter to the Secretary of State for Scotland, the Lord Privy Seal, the Secretary of State for Trade and Industry, the Chancellor of the Duchy of Lancaster, the Chief Secretary, Treasury and to Sir Robert Armstrong.

Yours ever
A handwritten signature in dark ink, consisting of several stylized, overlapping loops and a long horizontal stroke at the end.

Michael Heseltine

POSSIBLE REPHASING OF MISC 99 OFFER

The MISC 99 offer is:

	£m cash		
	1984-85	1985-86	1986-87
	17010	18040	<u>18464</u> *
Change on Treasury offer	+100	+106	<u>+111</u> *

* MISC 99 made no recommendation on 1986-87. This figure is a simple revaluation of 1985-86 by the 3% cash factor

2. The total extra across the three years is £317m but we do not believe that the MISC 99 phasing achieves the optimum effect either presentationally or managerially. If Mr Heseltine could be brought to accept that £317m extra is a final offer he might opt for rephasing. The Chancellor would not object to sensible rephasing.

3. At one extreme the whole £317m could be added to the final year giving:

16910	17934	18670
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This phasing would still give 3% real increases in 1984-85 and 1985-86 in fulfilment of the Government's commitment, and a non-Falklands cash increase in 1986-87 of 4.8%, well above the cash factor of 3%. (The Treasury would much prefer to talk solely in cash about 1986-87. My translation into "real terms" would derogate from cash planning and act as a ratchet in future years.)

4. A minimal rephasing would simply round down the earlier years in favour of the final year eg

17000	18000	18514
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There is a whole range of intermediate distributions.

5. The Treasury does not believe that Mr Heseltine will argue that pressure on the defence budget requires extra funds in the first two years. There are no signs of such pressure and the recently agreed flexibility arrangements will give further help. Any defence works and procurement underspend in 1983-84 can be carried forward into 1984-85 up to a maximum of £375m. No allowance is made for carry forward in any of the above figures.

6. At the bilaterals with the Chief Secretary, Mr Heseltine argued rather that it would be presentationally difficult for him to accept the Treasury proposals for the first two years, since the figures were below the 1983 White Paper published totals. The Treasury does not see
/ this

his as a major problem since the lower figures still provide for 3% pa real growth. The real issue is whether Mr Heseltine wants more than 3% real growth in 1984-85 coupled with a base 3% cash factor uplift in 1986-87, or whether he would prefer something closer to 3% in 1984-85 coupled with a cash increase in 1986-87 higher than the straight 3% revaluation.

8. Our conclusion is that an offer of some rephrasing of the MISC 99 offer could well prove attractive to Mr Heseltine. But he would first have to accept that it is redistribution not additional cash that is on offer.

Prime Minister

LEC NO

To be aware that there is still a disagreement about whether the inflation compensation formula should be published. The MISC 99 Secretaries have confirmed

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It was not discussed at MISC. Surely both that MoD does not parade its distinction from other programmes? But agree leave to parties for time being.

9 November 1983

9/11

Dear Secretary of State

I have seen your letter of 4 November to Willie Whitelaw.

I have accepted the formulation you propose, subject to the amendments we agreed with the Prime Minister on Friday evening.

At that meeting, we also discussed how the formulation should be interpreted. The letter of 7 November from the Prime Minister's private secretary to the Lord President's Office records the different views expressed and that you would consider whether you wished to pursue this.

Your letter also asks that the formulation be published with the Survey provision - presumably in the 1984 Public Expenditure White Paper. We did not discuss the possibility of publication in MISC 99 or on Friday, but I cannot agree that such a course is either necessary or desirable. My concern is that publication of the defence guarantee could not only detract from cash planning generally but also rebound adversely on other public expenditure plans or embarrass other colleagues. In view of this, I hope you can reconsider the matter; but if publication remains your preference, we might look at it again once we have agreed on how the formulation should be interpreted.

I am copying this letter to the Prime Minister, the Lord President, the Chancellor of the Exchequer and Sir Robert Armstrong.

Yours sincerely

J. A. G. G. G.

J. PETER REES

[Approved by the Chief Secretary]

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