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FROM: CHIEF SECRETARY

DATE: 29 July 1985

PRIME MINISTER

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R AND D PRIORITIES ACROSS GOVERNMENT

The postponement until 31 July of the E(A) discussion of priorities in government R and D allows me to comment on Sir Henry Chilver's letter to you of 2 July. I welcome the addition of the official report on Defence R and D (MISC 110) to the papers before E(A). It increases the need to pick out the main issues to focus on.

2 I agree with Henry Chilver that companies' R and D spending is a critical feature of our future competitiveness. It is not healthy that the share of industrial R and D financed by business itself is lower here than elsewhere, including the other countries where defence R and D is a high proportion of the total. It would be very serious if companies, as Henry Chilver says, are not responding to the improvements our policies have brought to the economic climate, and are failing to

"finance developments for the future out of increasing profits ... even though [they] are aware of the market opportunities offered by new technology and of overseas competitors' exploiting technology effectively."

3 We are unfortunately ill-informed about actual and planned expenditure on R and D by companies - no hard facts after 1983 - and though we have up-to-date information for the Government's own R and D spending and plans. This in itself may be a symptom of excessive concentration on Government subsidies for R and D rather than the key question of company motivation and performance. The only additional information

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on business R and D is partial: it is drawn from the accounts of those companies which choose to disclose their R and D expenditure. It is not necessarily representative, but the 15 companies reported £1.2 billion of R and D expenditure in 1983-84 about one-third of total company funded R and D in 1983. Between 1983-84 and 1984-85 these companies together reported an increase in R and D expenditure of 14 per cent. This does not bear out the gloomy impression given by the papers before E(A) about the performance of industry.

4 But if industry is not raising its R and D spending, then I agree with Henry Chilver that we must identify the reasons for that, and make these our target. On the picture he paints, I do not believe that simply putting more Government money into R and D will be a solution.

5 So far as our discussion next week is concerned, from the many issues raised I suggest:

- (a) that we should concentrate on priorities within government spending on R and D:
- (b) that the immediate issue is whether we accept the MISC 110 report and, if so, how it should be followed up;
- (c) that it may not be useful to spend much time on machinery, except what is needed for (b);
- (d) that we should commission DTI and Treasury officials to prepare a report covering what is known about companies' own spending on R and D and the influences on it; and the contribution which greater disclosure of such spending on the American model might make to changing attitudes in companies and financial institutions;

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6 I am sending copies of this minute to members of E(A); to those Ministers who will also attend on 31 July; and to Sir Robert Armstrong and to Sir Robin Nicholson.

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PETER REES

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MR ADDISON - No. 10

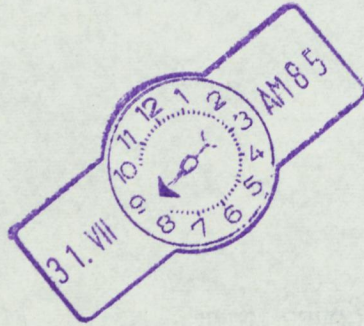
30 July 1985

R & D PRIORITIES ACROSS GOVERNMENT.

A short comment on the Chief Secretary's minute to the Prime Minister of 29 July. The figure of 14% increase in R & D expenditure for 15 companies between 1983-84 and 1984-85 is very misleading since it includes increases in R & D unit costs, mergers between companies etc. Between the same two years R & D expenditure as a percentage of turnover was either static or declined for most of the 15 companies whilst R & D expenditure as a percentage of profits declined for all companies except two. Therefore I am afraid the picture really is gloomy except, perhaps, for the electronics sector.

MSN

SIR ROBIN NICHOLSON
Chief Scientific Adviser



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