

P 01625

PRIME MINISTER

E(A)(85)18th MEETING AT 4PM ON 31 JULY
PAPERS ON GOVERNMENT RESEARCH AND DEVELOPMENT (R&D)

COVERS ITEMS 1+2

Sir Robin Nicholson and I have sent you detailed briefs on tomorrow's papers. But they are complex and controversial, and I thought it might help to send you these supplementary comments on overall handling and objectives.

2. It seems logical to take the items in the order suggested - civil R&D priorities first, and then the specific recommendations on Defence R&D in the MISC 110 Report.

CIVIL R&D PRIORITIES

3. On substance, it may be helpful to distinguish at the outset between Government spending and companies' own spending. Information on the latter is unreliable and out of date and you may wish to take up the Chief Secretary's proposal that the Treasury and DTI should examine this further. This might also cover the important points on financing innovation in Sir Henry Chilver's letter of 2 July.

4. On Government spending, if it is accepted that there is no need for an overall increase in Government civil R&D spending, then the key issues are those of direction and priorities. The main proposal is that greater priority should be given to wealth creation. As a general concept, like motherhood, spending Ministers will no doubt subscribe to this and claim they give it priority already. But if the Government really want to change priorities, some radical changes will be required which Departmental interests will strongly resist. This could involve a major change in the present customer/supplier relationship. Some R&D activity might have to be undertaken other than in pursuance of Departments' view of their own "needs"; and there would have to be a

specific mechanism for reallocating funds between Departments. It would also be most important to work out precise criteria that introduced effective economic tests and ensured that the Government did not subsidise R&D that could be better undertaken by the private sector.

5. If the Sub-Committee wish to move in this direction, then they will need to give a strong and explicit direction to enable effective follow-up action to be taken. There are two possibilities for such follow-up. One is the recommendation for a new (presumably junior) Ministerial Group to examine priorities etc. You will judge yourself whether this is likely to be effective. An alternative would be for the Cabinet Office, under Sir Robin Nicholson and myself, with the help of a strong steer to bring specific proposals back direct to E(A).


DEFENCE R&D (MISC 110 REPORT)

6. This report addresses the sore thumb in Government R&D - the £2 billion or so (over half the total) spent on defence R&D. This seems wholly disproportionate for a country of the UK's resources, and many of your colleagues have so commented in recent discussions (eg at Chequers).

7. The Report's conclusions are definite and radical and unlikely to commend themselves to the Secretary of State for Defence. They are, in essence, that:-

- the volume of defence R&D work should be decided collectively, and should be less than it is now;
- once the volume of defence R&D has been decided, machinery should be established to ensure that the needs of the civil economy are taken into account in specifying the characteristics of equipment to be developed and produced, and that spin-off to the civil economy is maximised.

In other words, a sharp cultural change in the control and direction of defence R&D. Not surprisingly, MOD have reserved their position on the report and indeed have been dragged very unwillingly to the water in the preparation of it.


CONFIDENTIAL

8. As my Chairman's covering note says, the Group was not so naive as to believe that if its recommendations were implemented, UK civil industry would be transformed overnight. They need a cultural change also. Sir Robin Nicholson's talks with companies have shown (as also Sir Ieuan Maddock's report to the NEDC some 3 years ago) that much of UK defence industry has become ossified and insulated and that means will have to be found, within the Government's economic and industrial policies, of encouraging it to adapt and take advantage of the commercial opportunities that could arise. The changes must, therefore, be gradual; but a start has to be made.

9. If the Sub-Committee endorse the Report's conclusions, we shall need a great deal of help from MOD and DTI in particular in working them up into a more precise set of proposals under the headings in paragraph 36 of the report. MISC 110 under the Cabinet Office seems the right vehicle for this; but it will need a strong and explicit steer if it is to achieve this.



J B UNWIN

Cabinet Office
30 July 1985