

Ref: A07304

CONFIDENTIAL

MR. WHITMORE

Prime Minister.
Agree no leak
enquiry?
Yes not
1/11/82

attached.

I expect that you will have seen the article on page 37 in The Economist of 30th January entitled "The Chancellor opens his Treasury books". It looks very like a leak of the Chancellor of the Exchequer's Cabinet paper on Economic Strategy.

2. I doubt whether the blame lies within the Treasury; drafts of the paper have been around for some time and one could have expected earlier leaks if they were going to come from the Treasury.

3. Internal evidence suggests the Department of Industry as a possible source: the last sentence of the 5th paragraph talks about the Department of Industry being "generally miserable about the way the Treasury has treated industry in its budget papers", and talks of Department of Industry officials planning to produce their own paper for Cabinet discussion. This would be consistent with a leak from the Department of Industry at or shortly before the time the Secretary of State for Industry sent round his letter indicating the help he thought the budget should give to industry.

4. But this speculation would be a flimsy basis for a conviction of guilt of the leak, and there are obviously other possibilities.

5. I have discussed with Sir Douglas Wass whether we should have a leak inquiry. We are against doing so. It is unlikely that it would disclose the culprit; Sir Douglas Wass does not feel that the article has done very much damage; and the very fact of instituting a leak inquiry would tend to confirm the accuracy of the article.

Robert Armstrong

1st February 1982

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BRITAIN



The chancellor opens his treasury books

Cabinet ministers trooped into Downing Street at 10am on Thursday for a novel experiment in British politics: the prime minister and the chancellor of the exchequer had decided to consult the cabinet about the budget (this year to be unveiled on March 9th). In the usual British way of budgets, most cabinet ministers have no idea what the chancellor has in store for them until a few hours before his budget speech. But Mrs Thatcher and her chancellor, Sir Geoffrey Howe, have been urged by backbench and cabinet critics to open the treasury books a bit this year and to consult them on budget options. The critics want to head off another hardline budget which would make life even more difficult for Tory members of parliament at the next election.

The treasury's somewhat flimsy background brief for cabinet discussion suggests that the gulf between the chancellor's intentions and the demands of the voters need not be too wide. It confirms that the chancellor has more elbow room for tax cuts or extra public spending than even he thought likely a few months ago.

The public sector borrowing requirement looks like being close to its £10.5 billion target for 1981-82. In the 1982-83 fiscal year, the treasury reckons Sir Geoffrey will be able to index income tax in line with inflation (along Rooker-Wise lines) and still meet his £9 billion PSBR target. That assumes excise duties are also increased in line with inflation and that the government sticks to its public spending plans as outlined in its recent white paper. Since these projections included a 4% "assumption" about public-sector pay which has already been broken by several major groups, spending totals could be higher than forecast next year.

Sir Geoffrey even suggests that a 1982-83 PSBR of £7 billion-8 billion (which would mean junking Rooker-Wise for the second year) would do most to impress the financial markets and help bring down interest rates. But that is just his opening bid in the budget talks. It makes his £9 billion offer look more reasonable and £10 billion positively generous.

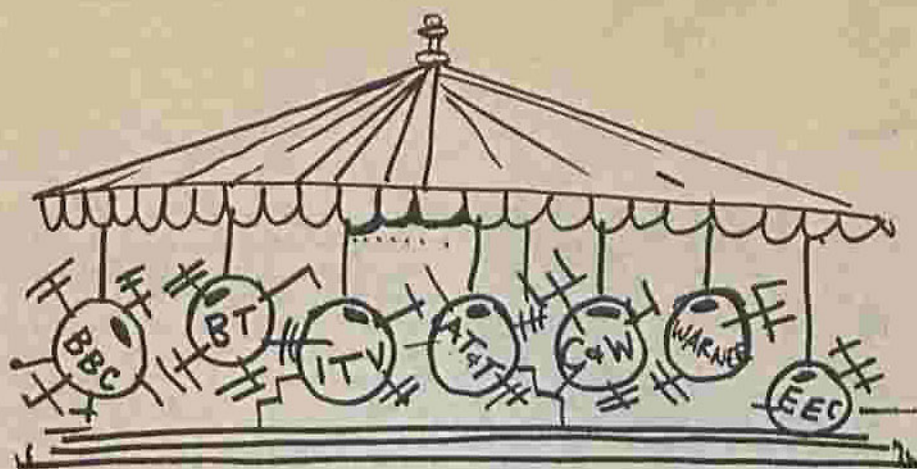
The cabinet was presented with three options for taking the PSBR into double

digits: income tax cuts in addition to indexing, which would keep Tory election promises; cuts in Vat and excise duties which would help cut prices; and specific help for industry, such as a cut in the national insurance surcharge, which might best reduce the jobless, now the main worry among even Tory voters. The industry department was happy to see the surcharge billed for a possible cut, but it is generally miserable about the way the treasury has treated industry in its budget papers. So department officials are planning to produce their own paper for cabinet discussion.

The chancellor holds out the hope of reasonable growth in 1983, inflation down to around 8% and unemployment falling. But he warns that this modestly rosy future could be destroyed by inflationary wage claims or continued high interest rates (fuelled from America or by a giveaway budget in March). He reckons that high interest rates on Wall Street (where they are likely to stay high after this week's state of the union message) are an extra reason for keeping a tight grip on Britain's PSBR, otherwise there would be little prospect of bringing Britain's rates down, and every chance of them going higher. Sir Geoffrey is also telling his cabinet colleagues these days that the exchange rate for sterling is just as important as the monetary aggregates.

The cabinet wets went into Thursday's meeting without a co-ordinated plan of attack. Many leading critics have piped down in recent months. Mr Jim Prior is busying himself with Northern Ireland. Others, such as Lord Carrington, rarely speak up on economic affairs. Not all of them speak openly to each other about budget matters anyway. On Thursday morning cabinet critics were uncertain about how genuine the consultation was meant to be. Budget discussion was fitted into a normal cabinet agenda, which meant that, after remarks by the chancellor and the prime minister, there would only be time for a quick run round the table, giving each minister perhaps three or four minutes to express his view.

The fact that Sir Geoffrey may now be gearing up for a 1982-83 PSBR of between £10 billion and £11 billion means that he will have room to do some of the things they have been clamouring for anyway: indexing income tax cuts and cutting the national insurance surcharge have been at the top of most of their lists.



Who dares hop aboard Britsat?

Any British government which drags the country into the new era of electronic information will do for Britain's industry in the 1980s what the railways did for it early last century. The Thatcher government, with its liking for the free-market and its need to get unemployment down from 3m, has better credentials and greater cause than most to try it. It started, but already seems to be losing its nerve.

Breaking the grip of the old Post Office monopoly last year was the easy part. Information societies flourish best when a thousand flowers are allowed to bloom. In corporate Britain that is not so easy to arrange.

This week the government's minister for information technology, Mr Kenneth Baker, had to intercede to persuade British Telecom (the new name for the telecommunications side of the old Post Office) to be kinder to Cable and Wireless. Cable and Wireless was the recently privatised company which the industry department picked last year to compete with BT's trunk telephone network. It wanted BT to guarantee international connections at decent rates. The company froze its Project Mercury (an optical-fibre communications link) in the face of tough bargaining by BT.

The government leaned on BT after Cable and Wireless complained. No doubt BT was trying too hard to protect its monopoly of connections to the rest of the world. Equally Cable and Wireless has for generations been in the highly political business of imperial and foreign communications. Its first instinct is not to drive hard bargains in the marketplace, but to squeal for ministerial help. After three years of Tory rule, the future of Britain's information technology is still substantially in the hands of companies which have been state-owned for so long that they have not yet unlearned the ways of state ownership.

Cable and Wireless is now set to re-

ceive its operating licence from the government to compete with BT on trunk routes. It is a slow start to establishing a new fast-track private communications network to satisfy business complaints about BT's services—especially from the City, which fears being left behind by other financial markets in the world of increasingly high-speed money.

The industry department's faces would have been even redder, however, had Cable and Wireless pulled out of Project Mercury altogether. In a free-enterprise world that would have given the government an excuse to let in American Telephone & Telegraph, the deregulated American monopoly now about to burst into world markets. Britain could benefit from its vigour and technology. But British Telecom would have been vulnerable. The Thatcher government believes in competition, but not that much.

Another tough decision in the government's in-tray is the all-British direct broadcast satellite. The home office is about to announce that it wants Britain to move quickly into this area: large, powerful satellites that can broadcast television programmes straight into people's homes. It will invite applications for a television satellite, to be launched by 1986, to provide two national television channels plus plenty of spare capacity for telecommunications circuits.

The cost of hopping on Britsat will be around £150m. The government says there will be no help from the public purse. But France, West Germany and

Luxembourg are keen to go with direct-broadcast satellites of their own. The usual British indecision would leave the country overshadowed by their beams and give the Europeans a head start in satellite manufacture. The opportunity lost could be very large: the position in the earth's orbit allocated to Britain under international rules for broadcast satellites (way out over the Atlantic) has commercial advantages which most continental allocations, more to the east, lack—the entire eastern half of the United States, from New Orleans to Chicago, would fall within Britain's beam.

Plenty of British firms are sniffing around Britsat, but each is waiting for the other to make a firm offer. As the official regulating agency, the home office is having to play marriage broker. The most ardent suitor is British Aerospace. It is anxious to manufacture the Britsat system (two in orbit and a spare on the ground) as its showcase to other countries buying broadcast satellites over the next two decades.

It would adapt a version of the European Communications Satellite (ECS), that it is already making for Eutelsat, the European consortium of public telecommunications authorities. Work on Britsat could begin as soon as it has the home office licence. GEC-Marconi is ready to collaborate by providing the business systems payload; N. M. Rothschild is ready with the money.

Who would use Britsat? British Telecom for one. It would use the telecommunications circuits, amounting to perhaps a third of the satellite's capacity, and shoulder a third of the costs. Then, dead stop. BAe and BT will not go ahead unless they get firm guarantees from Britain's two broadcasting organisations. Back to the home office: the BBC and the Independent Broadcasting Authority (IBA) cannot make a move until the home office decides how it wants the tv