

✓ Disposal of
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Defence

Ref. A04026

PRIME MINISTER

Defence Estimates 1981-82
Flotation of British Aerospace

The Secretary of State for Defence sent you a minute and proposed Parliamentary statement on this subject on 16th January, which you will be considering at a meeting this afternoon. The Secretary of State for Industry has sent you a minute today on the relevance of this statement to the flotation of British Aerospace in February - see paragraphs 5-7 below.

2. The positive tone of the proposed statement is clearly the best way to tackle a difficult task. The big question about this particular approach is how it will affect our allies, particularly the United States. You will wish to take careful account of the views of the Foreign and Commonwealth Secretary on this crucial point. It is obviously to our advantage to get this statement out as long as possible before your visit to Washington in February. I can see why Mr. Nott wants to make the statement tomorrow. But you will want to consider with the Foreign and Commonwealth Secretary and the Secretary of State for Defence whether the timing is right vis-a-vis the Americans. Mr. Reagan will be concentrating on his inauguration tomorrow, and is unlikely to think about the statement at once. But its implications will undoubtedly be drawn to his attention: is there a danger that he may think that we timed the statement for Inauguration Day in the hope that he would be too busy to notice it?

3. On the substance of the statement itself, there are two general points of a positive nature which you may like to suggest should receive greater emphasis:

- (1) As one of the problems confronting the defence programme this year has been the accelerated level of deliveries from industry, there is an opportunity to deal with this phenomenon in more constructive terms than those used in paragraph 5 of the draft. Could the Secretary of State for Defence pay British industry the compliment of suggesting that part of his immediate cash flow problem stems from the over-prompt deliveries which he has been receiving from industry - which is a pleasant contrast to the accusations of late deliveries which are so often levelled at British companies?

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(2) The other positive point to which he might give greater emphasis is the fact that the proposed reductions will have little impact on the manning and equipment of the British Army of the Rhine, which is the British contribution to NATO to which our allies including the United States attach most importance. This point could be injected into paragraph 4 of the draft statement, which mentions a number of improvements which have been made in the defence programme in more general terms.

4. There is also one point of detail which you may care to suggest. I understand that No. 41 Commando is at present seriously undermanned. It might be worth mentioning this fact, if the Secretary of State for Defence can confirm its accuracy, to underline the statement that its merger with the other Commandos will not reduce the effective overall strength of the Royal Marines.

British Aerospace

5. The problem of dealing in the sales prospectus with the implications of the defence programme for British Aerospace is discussed in the minute of 7th January from the Minister of State, Department of Industry, to you and in the Secretary of State for Defence's minute to you of 16th January. There are two points in particular in the present draft statement which worry the Secretary of State for Industry:-

- (i) Paragraph 4 states that "Contrary to some reports, development work on the Sea-Eagle anti-ship missile will continue" - misleading because the possibility of cancellation is not ruled out (see paragraph 4 of the Secretary of State for Defence's minute to you).
- (ii) Paragraph 8 states "We must, over the next year or so, look realistically at our programmes to see what needs to be done" - satisfactory if it refers to the normal, ongoing process of review but difficult if it implies some more radical exercise.

The Secretary of State for Industry will, I understand, suggest drafting changes which could meet these points. He will copy his minute to the Attorney General and probably suggest that he should come to the meeting to advise on these questions.

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6. If the Secretary of State for Industry's points cannot be readily met, that adds to the case for deferring the statement until the issues can properly be thrashed out.

7. If, on the other hand, amendments can be made and it is accepted that there are no further defence problems for the British Aerospace prospectus, the way is clear for flotation subject to two points:-

(i) The Chancellor of the Exchequer accepting that February flotation should not be held up to enable a review of the BAe 146 aircraft to go ahead - the Financial Secretary appears to have accepted this in his letter of 12th January to Mr. Tebbit.

(ii) Your being satisfied that the sale of half the shares should go ahead for a net return to the Government estimated to be in the range of £15-£30 million - this is discussed in more detail in paragraphs 3 and 4 of the minute of 12th December to you from the Secretary of State for Industry in which he reported the recommendation of E(DL) that the Government should continue to aim for flotation as soon as possible in spite of the relatively low return.

ReA

ROBERT ARMSTRONG

19th January, 1981

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