11th January, 1968

CABINET

PUBLIC EXPENDITURE: POST-DEVALUATION MEASURES

DEFENCE CUTS: THE F. 111

Memorandum by the Secretary of State for Defence

When we discussed the F. 111 last week, the Cabinet (CC(68) 1st Conclusions, Minute 3) invited me to propose alternative economies with a view to securing defence savings comparable with those which I could make if the whole F. 111 order were cancelled.

The Gross Saving from Cancellation

2. On the assumption that our withdrawal from East of Suez is completed by April, 1971 I can reduce the defence budget from £1,890 million in 1968-69 to £1,650 million in 1972-73 (at 1964 prices) while keeping the 50 F. 111s and 170 Phantoms now on order. This saving would be reduced by £10 million if withdrawal is not completed until April, 1972. The impact on all three Services will be severe and rapid, though it will take some time to work out the consequences in detail. By the early 1970s there will be massive cuts in the numbers of fighting units. The size of the forces will be cut by 80,000 - representing an immense transfer of manpower to the civil sector - equivalent, with their families, to a town the size of Newcastle or Leicester. Apart from a radical reduction in the whole support organisation we shall have cuts in many "teeth" areas, including the aircraft carriers and the rate of new naval building; cuts in the number and organisation of regiments and battalions; cuts in the transport and maritime forces of the RAF and the elimination of the proposed VG combat aircraft. Against this background, if we are to maintain effective volunteer forces at all, the remainder must know they will have good conditions of service and such new equipment as is essential for their tasks.

3. If our reduced forces are to be given no protection whatever against the consequences of losing a strike/reconnaissance capability on which they have depended since the invention of the flying machine, and our NATO allies are prepared to see us remove all their best reconnaissance aircraft and an essential part of their longer-range strike force without making any compensatory increase in our contribution in other fields, cancellation of the F. 111 order would save an average of £39 million a year or £390 million in all up till 1977-78, though owing to the incidence of credit repayments the saving in 1972-73 would be £57 million.
4. On the other hand, owing to cancellation charges our expenditure next year on the F. 111 would increase from £16 million to £38 million, £33 million of which would be in dollars. We would also lose the substantial benefits under the offset agreement which I described in C(68) 10, and which ensure that if we keep the 50 F. 111s, we shall earn at least $50 million more than we pay over the next three years. Annex A to this paper deals more fully with arguments against the offset agreement which were used by some of my colleagues at our meeting of 4th January.

The Military capability lost by Cancellation

5. The unanimous view of all four Chiefs of Staff on the importance of the F. 111 to all three Services is summarised in the following statement: "The heart of the case for the quality of long-range strike and reconnaissance capability represented by the F. 111 is that, broadly speaking, all other operations of war short of ultimate strategic nuclear attack take place either under cover of this capability or with the knowledge that we have it at our disposal if necessary. If this capability is abandoned then our sea, land and air forces are not only deprived of the ability to find out by reconnaissance what an enemy or potential enemy is doing, or is planning to do, but are also thrown back on an essentially defensive strategy with all that this means in surrender of the initiative. The loss of the F. 111 would, therefore, carry the gravest military implications for the United Kingdom's ability to participate in military operations in Europe and overseas and remove an element of real significance in the process of control of escalation".

6. I described in C(68) 10 the critical importance of the F. 111's strike capability in reducing NATO's reliance on nuclear weapons. I would like here to re-emphasise the importance of reconnaissance, not only in saving the lives of our fighting men, but also in checking the escalation of a crisis. Once we received intelligence that something was afoot we should want to have the most accurate information possible before deciding how to react. Aerial reconnaissance is the prime source of such information. The F. 111 has two special attributes as a reconnaissance aircraft, one of which is possessed by no other aircraft planned for service in Europe; without crossing national boundaries it will be able to look "sideways" with camera and radar from about 100 miles from within friendly air space or from international waters. If, however, at a later stage in the crisis fighting has started, the F. 111 can pass over national boundaries, and its chances of being able to do so and return, whatever the weather conditions, are much greater than that of any other aircraft because of its supersonic speed, range and sophisticated electronic fit.

7. The Phantom offers no alternative. It is essentially an aircraft for operating in the battlefield area. It lacks the unique and valuable "sideways"-looking photographic facility. In the reconnaissance role it has not the performance at the relevant heights, it is limited in bad weather and its range is only a quarter that of the F. 111. To give the Buccaneer an analogous but much inferior reconnaissance capability would take some seven years at a programme cost no less than that of the F. 111A which would otherwise have replaced the Canberra some five years earlier.
When we originally reduced our F.111 order from 110 to 50, we assumed that they would supplement some 150 AFVG, coming into service primarily in Europe from 1975 onwards. The AFVG project collapsed last year, and it is now clear that there is no chance of collaborating in a UKVG aircraft in the same timescale. This has given a new importance to the 50 F.111, particularly in Europe.

8. For Britain to depend wholly on the United States and France providing aircraft for vital information in a crisis would gravely damage our political influence on events, quite apart from its military consequences.

9. The reconnaissance and strike capability could be equally important outside Europe both in the final stages of our withdrawal and in any operations we might undertake thereafter. Indeed it is clear that if our general capability in Europe does not include the F.111, our declared readiness to help outside Europe if we believe it our duty or interest to do so will be worth very little to those whose acquiescence in our withdrawal we are now seeking.

Our contribution to NATO

10. As I understand it, one purpose of our withdrawal into Europe is to maximise our influence with our continental neighbours, an objective of paramount importance whatever our relationship with the Common Market. I do not believe it would be politically possible or desirable to rob NATO of the 36 front-line F.111 (which is what a buy of 50 will permit) we have already promised, in replacement for the 100 Canberras assigned to NATO and the further 50 Canberras available to NATO in a crisis, without making some increase in our air contribution to compensate for their loss.

11. The tables at Annex B show how our own projected defence programme in 1972-73 will compare with that of France and Germany both in terms of money and of forces provided for West European defence.

12. The force figures show that without the F.111 contribution our effort in the common defence would compare more closely with that of Holland than with France or Germany. The expenditure figures (which are on the NATO definition for purposes of comparability and include, e.g. military aid) show that on the basis of present plans our total expenditure in 1972-73 would be some £4-500 million lower than that of France or Germany (even before taking account of the latter’s heavy expenditure - some £275 million - on the support of Berlin). On the basis of expenditure per head of population, the figures would be:

| Country  | £
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<tbody>
<tr>
<td>United Kingdom</td>
<td>36</td>
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<tr>
<td>France</td>
<td>50</td>
</tr>
<tr>
<td>Germany</td>
<td>40</td>
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The disparity would still be significant if the F.111 were included in our programme.
13. A big increase in our land contribution is undesirable on many grounds - including the additional foreign exchange expenditure and the doubt whether we could achieve it without conscription. There is no case for increasing our naval contribution. Any increase to compensate for loss of the F. 111 would have to be made in aircraft.

14. At present the total number of combat aircraft we declare to NATO is 223. In 1972 without the 36 F. 111s it would amount to only 100 aircraft (including 32 IV bombers whose operational value is steadily waning). In my view, there is no possibility of persuading our allies that a reduction on this scale, when we have disengaged from East of Suez and at a time when NATO strategy is being revised - at our urging - to lay greater stress on the flexibility of conventional air power, justifies the claim that we are bearing anything like our fair share of the defence burden. The German aircraft contribution would be several times larger than ours, while their Army contribution was five times greater. We should be offering fewer aircraft than Italy and at the best the same numerical order as the Dutch and the Belgians. Above all, the argument that we were making up in quality for a reduction in quantity would have been removed.

15. Both from the point of view of general capability and our relations with NATO, the work I have done suggests that if we have no F. 111's the least unsatisfactory course would be to buy at least a further 75 Phantoms. These 75 Phantoms would produce a front line of some 50 to supplement the 20 already assigned to NATO and the 20 which would later become available to NATO from the Gulf and Far East. Besides being the only aircraft available when the Canberra's are withdrawn next year, the Phantom's ability to shoot down enemy aircraft in the air would do something to compensate for ending our ability to destroy enemy aircraft more cheaply and effectively on the ground. Although in general it could be said that 50 Phantoms can carry about the same weight of weapons as 36 F. 111s, this is not a meaningful comparison. Because of the quite different performance characteristics of the Phantom, in particular its inferior reconnaissance capability, its inability to strike in all weathers, and its shorter range, the overall operational effectiveness of our contribution would be greatly reduced, even if we substituted this larger number of aircraft.

16. The 10-year cost of 75 Phantoms required would be £275 million of which the dollar content would be £118 million and the additional DM stationing costs £12 million. The budgetary cost in 1972-73 would be £34 million. Apart from these financial implications, there would be other serious implications not least for the future of our aircraft industry.

The net savings from cancellation of the F. 111

17. I therefore assume that we should have to add back some £275 million over the 10-year period to pay for an additional 75 Phantoms. The net saving we should secure by cancelling the F. 111 would therefore be £115 million over the 10-year period and £23 million in 1972-73.
How to find a comparable saving

18. (a) Forces in Germany

An unknown factor in the equation is the extent to which we may reduce our forces in Germany before 1972 either because we are unable to make a satisfactory offset arrangement or because our allies cut their forces or because there are reciprocal reductions on both sides of the Iron Curtain. However, we cannot quantify such savings, still less announce them now - a problem which arises similarly from our general intention to introduce selectivity into family allowances.

(b) Restructuring of the Services

If concrete savings must be identified, the right way to do it, as I argued in C(68) 11, is to re-examine the whole of our force structure and support organisation in the light of our more rapid withdrawal into Europe, but it will take several months to do so. I can certainly undertake to find savings in 1972-73 to fill the gap - as I have found all the savings required of me on four previous occasions.

(c) Immediate possibilities

If however, my colleagues decide that for presentational reasons the Government must be able to announce specific further cuts in defence next week even though this might turn out to produce less desirable savings than a thorough study would allow, my views would be as follows:-

(i) I would not propose cutting or cancelling the Harrier order, because though it has a low military priority I believe the general advantages of continuing the only British advanced combat aircraft now take precedence.

(ii) I would propose to cancel the order for the Anglo-French Martel missile, thus saving £79 million in 10 years and £17 million in 1972-73. The implications of this cut are explained in Annex C.

(iii) To find the balance of the comparable saving of £23 million in 1972-73 I would choose between the abandonment of the Bloodhound system (£2 million), phasing out some of the V-bombers more quickly (up to £10 million) and stopping research and development on an Airborne Early Warning (AEW) aircraft (£7 million). There are almost certainly other possibilities. Any of these cuts would be painful and unwelcome but they are in my view areas of less critical importance than the F.111 capability.

-5-
19. It may be suggested that the argument in paragraphs 15-17 about the net as opposed to the gross saving is unacceptable. I strongly disagree; although I acknowledge that in the short time available the assessment of a compensating capability could only be rough and ready. Some may say it is too big. Some may argue that it should not be made at all although this can only be tantamount to asking me to find another £390 million off the defence budget over the next 10 years in addition to the cuts which already reduce the programme to £1,650 million in 1972-73. This would be a still more difficult and speculative task and inevitably involves looking forward into the second five years (1973-1978) of the period as there is such a long lead time in the defence procurement areas.

20. I have been able to examine such a proposition only very cursorily. The area I have indicated in paragraph 18(c)(ii) and (iii) would save at least £100 million in the first five years. Their continued effect, together with the elimination of firm assumptions in our 10-year costings such as the purchase of United States C5 transport aircraft and a United Kingdom built AEW aircraft in the second five years, would result in a total saving of some £400 million equivalent to the gross cost of the F.111 programme less only cancellation charges. I quote these only for illustrative purposes, but here again I can assure my colleagues that I would be prepared to forgo these or other items as of less importance, both short and long term, than the F.111's contribution to our military capability and credibility.

Conclusions

21. I conclude that:

(a) To eliminate the F.111 from our defence programme without replacement would put our fighting men at risk and seriously damage our political and military influence in NATO.

(b) It would also mean spending an additional $60 million in 1968-69 and losing the advantages of the $825 million offset target I have just negotiated.

(c) There is no aircraft available which could replace the Canberras from 1969 and provide an equivalent military capability. The nearest substitute would be the Phantom. The programme costs of 75 Phantoms would amount to some £275 million compared with the next F.111 saving of £390 million. The comparable saving that I set myself to find is therefore £115 million, of which £23 million would fall in 1972-73.

(d) I could guarantee to find this comparable saving in the course of restructuring the forces following upon our decisions on commitments.

(e) If there is a desire for presentational reasons that I should identify these savings now, my proposals are set out in paragraph 18(c)(ii) and (iii). These cuts include a complete and publicly known weapons system, Martel, which we are currently undertaking in collaboration with France.
(f) If we ignore the costs of any substitution programme and take the ten year gross costs of the F. 111 programme less cancellation costs - £390 million - I could guarantee to find savings over the 10-year defence budget. Such savings would include those in (e) above and would go on in the second half of the 10-year period to include the elimination of such major new equipment purchases currently in the programme as the United States C5 transport aircraft and the construction of an AEW aircraft.

Recommendation

22. I therefore recommend my colleagues to confirm the purchase of 50 F. 111s.

D. W. H.

Ministry of Defence S. W. 1.

11th January, 1968
The Offset Arrangement

1. Some of the arguments used at the last meeting to write down the value of the offset arrangement seem to me to be unsound and I seek in the following paragraphs to explain the position as I see it.

2. It was argued that "export earnings under the agreement did not bring in net benefit to the balance of payments; they simply prevented the deterioration which would otherwise result from purchase of the aircraft". This argument I do not accept. We cancelled the TSR 2 partly because it was not going to be ready in time, partly because of its very high and rapidly escalating cost and partly to diversify resources to civil industry, thus benefitting the economy. It was implicit in that decision that a foreign aircraft would have to be bought in its place, since there was no other British aircraft in prospect that could meet the requirement. Indeed the P.111 was the only aircraft that could do so. It was because I was conscious that this unavoidable purchase would involve expenditure in foreign exchange that I obtained the offset arrangement. It would have been unrealistic to expect the Americans to undertake to do more than offset its cost; but, as shown below, there is a good chance that they may in the long run do much more than merely "prevent deterioration". Meanwhile, during the immediate future, the receipts from sales to America under the offset are considerably exceeding the payments to be made for the P.111.

3. It was argued that "there was a good prospect that the industrial resources now devoted to securing sales under the offset agreement could be diverted to exports which would bring a positive balance of payments benefit". I should like to see some positive evidence to support this statement. The facts are that during the 4 or 5 years preceding the signing of the offset arrangement the US defence market had been virtually closed to our industries. Under the Buy American Acts, foreign competitors had long suffered a discrimination of 6% (or in some cases 12%) as compared with the American producer; and this applied to all US Government competitions. In 1950 the US Department of Defense introduced a price-differential of 50% inclusive of duty which could be applied in the defence field whenever it gave a more penal handicap to the foreign competitor than the 6% or 12% plus duty. These restrictions made it virtually impossible for British firms to obtain defence contracts in the United States unless the US has no source of their own or for some special reason wanted to buy abroad. What the offset arrangement did was to break down these barriers and give British firms once more an opportunity of competing for contracts on equal terms with the Americans. Moreover the American Forces were instructed to search out British equipment which would be suitable for their needs and to provide opportunities for British companies to tender for contracts. I am sure my colleagues will agree with me in attaching importance to maintaining access for as many British industries as possible to the enormous US market. Over 14% of our exports go to the United States, which is nearly three times as much as we export to any other country. This seems to indicate that maintaining access to the US defence market for as long as possible must be in itself beneficial and more worthwhile than seeking to transfer the effort to other exports which in may event we are doing all
we can to obtain. Firms such as Elliott Automation who get their feet in the American door have a chance of establishing production lines out of all proportion to those appropriate for other markets. The competition is healthy for both countries: the Americans benefit from reduced prices even when the British firm does not win and the British firms have valuable lessons to learn from the high standards of American competition.

4. It was argued that gaining a foothold in the US market was "of limited advantage, since it was certain that, once the target for offset sales had been reached, the barriers to sales in the United States would immediately re-appear". I do not know on what evidence this statement is based. The Americans obviously could not make the offset arrangement open-ended; and they have naturally been cautious about public statements. There is, however, good reason to suppose that the target figure will be exceeded. Moreover, before the target (including the extra $100 million) is reached, the US balance of payments may improve, in which case the 50% price-differential would be removed since the American Forces would be glad to make the budgetary savings which access to our highly competitive products would afford. In any event the arrangement is due to run for nearly 10 more years.

5. Finally, the provisions of the offset arrangement dealing with collaborative sales have already given us access to a market hitherto regarded as a US preserve; this would also be true of any further collaborative sales, for otherwise we should not accept them as truly collaborative.
### ANNEX B

#### COMPARISON OF EUROPEAN DEFENCE EXPENDITURE

**A. Expenditure**

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<td>1. (a) UK Defence Budget</td>
<td>£M</td>
<td>2,385</td>
<td>2,320</td>
<td>2,250</td>
<td>2,190</td>
<td>2,065</td>
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<tr>
<td>(b) per head of population</td>
<td>£/per head</td>
<td>43</td>
<td>41</td>
<td>40</td>
<td>38</td>
<td>36</td>
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<tr>
<td>2. (a) French Defence Budget</td>
<td>£M</td>
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<td>2,550</td>
<td>2,550</td>
<td>2,550</td>
<td>2,550</td>
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<tr>
<td>(b) per head of population</td>
<td>£/per head</td>
<td>49</td>
<td>51</td>
<td>50</td>
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<td>50</td>
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<tr>
<td>3. (a) W. German Defence Budget</td>
<td>£M</td>
<td>2,130</td>
<td>2,210</td>
<td>2,310</td>
<td>2,380</td>
<td>2,470</td>
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<tr>
<td>(b) per head of population</td>
<td>£/per head</td>
<td>35</td>
<td>36</td>
<td>33</td>
<td>39</td>
<td>40</td>
</tr>
</tbody>
</table>

(i) UK figures are based on NATO definitions.

(ii) Population figures for all 3 countries projected at the annual UK rate of increase of 0.72% assumed in the National Plan.

(iii) Record of meeting held between S. of S. and French Minister of the Armed Forces on 26th October, 1967. Increased expenditure of 30 milliard francs in 1969/70 assumed to remain at that level from thereon.

(iv) W. German reply to the Questionnaire for the 1967 Defence Planning Review.
### B. Force Proposals 1972

(UK figures as reported but modified to take account of latest cuts, and excluding F III)

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<thead>
<tr>
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<th>W. Germany</th>
<th>Holland</th>
<th>France</th>
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<tr>
<td>Armoured</td>
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<td>31</td>
<td>10</td>
<td>15</td>
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<tr>
<td>Mechanised</td>
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<tr>
<td>Other brigades</td>
<td></td>
<td>6</td>
<td>3</td>
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<tr>
<td><strong>NAVY</strong></td>
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<tr>
<td>(Categories A &amp; B)</td>
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<tr>
<td>Aircraft Carriers</td>
<td>2^</td>
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<td>1</td>
<td>3</td>
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<tr>
<td>Cruisers, Destroyers, escorts</td>
<td>63</td>
<td>19</td>
<td>24</td>
<td>49</td>
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<tr>
<td>SSBN</td>
<td>3</td>
<td>-</td>
<td>-</td>
<td>3</td>
</tr>
<tr>
<td>Other submarines</td>
<td>23</td>
<td>18</td>
<td>6</td>
<td>21</td>
</tr>
<tr>
<td>Maritime patrol aircraft</td>
<td>30</td>
<td>20</td>
<td>12</td>
<td>80</td>
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<tr>
<td><strong>AIR FORCE</strong></td>
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<tr>
<td>Fighter/bomber</td>
<td>44</td>
<td>180</td>
<td>79</td>
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<tr>
<td>Medium bomber</td>
<td>32</td>
<td>76</td>
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<td>175</td>
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<tr>
<td>Light strike</td>
<td>72</td>
<td>396</td>
<td>97</td>
<td></td>
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<tr>
<td>Fighter/Reconnaissance</td>
<td>32</td>
<td>76</td>
<td>72</td>
<td></td>
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<tr>
<td>All weather fighter</td>
<td>24</td>
<td>72</td>
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<td>75</td>
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<tr>
<td>SAM Units</td>
<td>1</td>
<td>15</td>
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<tr>
<td>SSN Units</td>
<td>-</td>
<td>4</td>
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* Figures for France are from Intelligence sources, France not having made any recent declaration to NATO. They exclude the non-naval element of the Force de Dissuasion, which will consist of about 50 bomber aircraft and 27 IRBM's.

+ Commando carriers
ANNEX C

Implications of Reducing or Abandoning the Martel Programme

The development of the Anglo/French Martel air-to-air guided missile, in both its anti-radar (AR) and television-guided (TV) versions, is nearing completion but we have not yet placed any production orders.

2. If we abandon Martel our strike aircraft will be without any stand-off capability for attacking defended targets both on land and at sea. They will be forced to use less accurate weapons and to approach the target more closely, thus increasing their vulnerability. Retention of the AR missile would allow radar targets to be attacked, which would be particularly useful at sea, but there would still be no stand-off capability against visual targets.

3. Abandonment of Martel might cause difficulties with the French who might find unwell the extra cost of developing and producing their own small requirements unilaterally and might be less willing to collaborate with us on other projects. They would be more likely to consider withdrawing from the helicopter programme than from Jaguar. Their withdrawal from the helicopters would be serious though not catastrophic.

4. On the other hand our judgment is that the French have strong motives of self interest (as we have) in continuing with both the Jaguar and helicopter programmes. On balance therefore, although the French might complain at being let down on Martel, particularly so soon after the signing of the Jaguar production agreement, there are reasonable chances that we might avoid any serious repercussions. The chances would be considerably increased if we could complete development of the weapon and continue with the AR programme.

5. Abandoning production of Martel completely would save about £75M in the ten-year period (£17M in 1972/73). Confining production to the AR requirement as currently stated would save about £50M (£13M in 1972/73).

6. Cancelling the development of Martel at this late stage would save only £26M out of the £25M which is the UK half share of the cost of the joint development programme, We could therefore complete development for a relatively small extra cost. This would:

   a. help considerably to avoid difficulties with the French which might affect other collaborative programmes;

   b. establish a stronger claim to a share of production to meet French requirements, although the share may not be large.

The savings quoted in the main paper assume that development is not completed.