START 22-02-83
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PART C

BUDGET BRIEFING 1983

D.D 25years NAzis 15/7/94

PART C

CLOSED

CONTINUED ON:-

PART D

BUDGET SECRET

FROM: E P KEMP
22 February 1983

MR KERR

Discussed w 25/2

We need to be v. cautious on this. PM is – + rightly so – keen on Family Supp (hence drive for 26.50 C.B.). So I shd certainly like * is indisputable. to follow §3 – which seems helpful. It is §4 is correct. It wd, moreover, be in order to bring the whole of NT's package I, A + B – in his reading, as he seems to me, to deal

BUDGET - BETTER OFF VERSUS THE REST

After this morning's meeting the Chancellor had some words with us about the "Budget for the better off" point. I attach for convenience a copy of my note of yesterday which set out some brief thoughts on this point. (The arithmetical exercise referred to at the end of paragraph 3 is still in hand. But it is not a very easy one and at the end of the day unlikely to be very convincing - as I say if any of these points are used by the Opposition they will be chosen selectively and on the basis of individual cases; I doubt if we shall get very far with overall numbers.)

TS 7WCS

2. Looking at the note again there are two further points which I should have included. First, I ought to have mentioned in paragraph 2 that there will be some people around one and a half times average earnings who will actually lose in cash terms on the static basis when NIC and income tax are taken together - while better off people (and, I agree, much less well off people) will gain; and second, going in the other direction, we shall, if things remain as now planned, be able to point to the restoration of the 5 per cent abatement on unemployment benefit. And of course the Chancellor said to us this morning that he did not think the point about not taxing the banks is one which we should worry about in this context.

3. Nevertheless I still think the potential indictment as a whole is a serious one. It is, if I may suggest it, a point relevant to the discussion at tomorrow morning on the social security problems. I see that Mr Monger's submission suggests that it might be possible to pay for the potential additional cost by ditching the whole of the "caring" package and then nibbling away at the proposed child benefit uprating. I really do think, in the context of not giving the Budget a "more for the better off" flavour, we ought to try to save the full caring package and the higher child benefit increase.

BUDGET SECRET

4. It is not as though, at least from the public expenditure point of view, that we seem to need to make savings that are all that rigorous. Sir Anthony Rawlinson's minute suggests he could take £350 million on the Contingency Reserve. Including the caring package and the full child benefit proposed and £25 million for employment measures, the amount at risk so far is only £262 million. Thus there is room for the additional £30 million, or even the additional £60 million, which might arise on the social security package. And there would be even more room if we could turn down the employment measures - though we really want to keep these on deck if we can because they go to help with the "businesses versus persons" problem.

E P KEMP

FROM: G W MONGER
DATE: 22 February 1983

CHANCELLOR

Meeting with Fowler
[illegible] Dudley

cc Chief Secretary
Sir D Wass
Sir A Rawlinson
Mr Bailey
Mr Middleton
Mr Evans
Mr Kemp
Mr Mountfield
Ms Seammen

SOCIAL SECURITY ADJUSTMENT

You asked for more detail on the financial implications of giving up the social security adjustment and returning to the historical basis of uprating in 1983.

2. The package of savings and sweeteners which we had in mind was as follows (£m):

	1983-84	1984-85
Saving from 2% adjustment	215	596
Sweeteners	35	78
Net Savings	180	518

The sweeteners were as follows:

Restoration of 5% abatement of UB	22	59
Increase in SB single payments limit	1	3
Increase in SB capital cut-off	2	8
War Pensioners' Mobility Supplement	0	2
Increase in Mobility Allowance	2	6
Increase in Therapeutic Earnings Limit for incapacity benefit	0	0
Removal of invalidity trap	7	23*
	35	101 (78 net)

* Cost of removing invalidity trap was to be met by savings on housing benefit in 1984-85 onwards.

Cost of the Decision on Historical Uprating

3. The cost of a decision to abandon the adjustment and return to the historical basis of uprating depends on the difference between:

i. The uprating in November 1983 on the old forecast basis less the 2% adjustment; and

ii. This uprating, based on actual inflation in the 12 months to May or June 1983.

The latest forecast for i. is 6%, giving an uprating of 4% after the adjustment. For ii. the latest forecast is 4¼%. The extra ¼% on the uprating would cost about £30m in 1983-84 and £90m in a full year. But it must be emphasised that the outturn for May is still very uncertain, within a range of about 1%. The forecast for November to be made in the Budget is also still unsettled. There is therefore a very wide range of possible outcomes.

4. It is for Mr Fowler to say whether it would be practical to base the uprating on the June RPI, but DHSS officials think it would not be. The present best forecast of the June RPI is 4½%. The extra ½% produced by such an uprating would cost (again as compared with our original package) £60m in 1983-84 and £180m in 1984-85.

5. There would be a further small cost on public service pensions, but within the margin of error. A ¼% increase in their uprating would cost an extra £1-2m in 1983-84 and £4m in 1984-85.

6. All these costs would fall on the Contingency Reserve.

Offsetting Savings

7. A possible aim would be to make savings to offset the additional cost of the Prime Minister's proposals. This indicates making savings in the range £30-60m in 1983-84 and £90-180m in 1984-85, the top of the range reflecting both the risks created by the general uncertainty of the figures and the possibility that the uprating will be based on the June RPI.

8. The first question to decide is whether the proposed restoration of the 5% abatement in UB can be given up. You said this morning that this restoration was unavoidable and indeed there is intense pressure for it. There is the possibility, mentioned by Mr Fowler, that the extra uprating of UB could be held to 2.3%, on the ground that it enjoyed last year's overshoot of 2.7%. This would save about £12m in 1983-84 and £33m in 1984-85. But it must be very doubtful whether such a course would be politically realistic.

9. Apart from this possibility, the savings can come only from giving up the sweeteners in the Caring Package, and reducing the uprating of Child Benefit. On the assumption that all the Caring Package sweeteners are given up:

i. To achieve savings at the bottom of the range (£30m in 1983-84, £90m in 1984-85) would mean cutting back the new level of CB from £6.50 to £6.40.

ii. To achieve savings at the top of the range (£60m in 1983-84, £180m in 1984-85) would mean cutting back the new level of CB to about £6.25.

The figure of £6.40 would restore the April 1979 value on the (unrealistic) assumption that inflation between November 1982 and November 1983 is 5%. There is no way in which a figure of £6.25 could be represented as restoring the April 1979 value. There would also be the relationship with tax allowances to consider.

10. One Parent Benefit would presumably be treated in the same way as Child Benefit. The sums at stake are very small.

11. There is one other possible source of savings: the savings on housing benefit, which amount to £5m in 1983-84 and £30m or more in 1984-85. We had originally agreed with DHSS that these could be partly used to finance removal of the invalidity trap, if they could keep the remainder, mainly to increase the housing benefit children's needs allowance. It would be possible either to confiscate these completely - which would be very difficult - or to use them in part to finance removal of the invalidity trap, or other items in the caring package.

Other Economic Assumptions

12. There are two possible changes in economic assumptions which will affect figures for social security expenditure in the White Paper:

i. A higher assumption about inflation producing a 6% uprating in November on the forecast basis rather than the 5% assumed in the White Paper: cost £100m in 1983-84, £300m in a full year.

ii. A lower assumption about unemployment than in the White Paper, producing a saving of £100m in both 1983-84 and a full year.

These changes are independent of the decision reached yesterday, and are not therefore considered in more detail. They would count as estimating changes and the costs would not be met out of the Reserve.

G W MONGER

CONFIDENTIAL

From: Sir A Rawlinson
Date. 22 February 1983

CHIEF SECRETARY

MWT

cc Chancellor of the Exchequer
Sir Douglas Wass
Mr Burns
Mr Middleton
Mr Bailey
Mr Wilding
Mr Mountfield
Mr H Evans
Mr Lovell
Mr Monger
Mr Burgner
Mr Kemp
Mr Cassell
Mr Ridley
Mr Kelly

BUDGET: PUBLIC EXPENDITURE

This minute looks at the public expenditure aspects of the Budget in the light of the discussions on 21 and 22 February. It replaces my minute of 21 February.

2. Mr Monger is putting up a separate note discussing the social security items, including child benefit and the public expenditure items in the caring package.

3. The policy decisions on these items, in so far as different from what was in the public expenditure White Paper, should be charged to the Contingency Reserve.

4. In addition to whatever is decided for these items, we now have for the Budget the following items to be charged to the Reserve for 1983-84:

		£m
Employment measures (Early retirement, Enterprise allowances)		25
Construction		85
Comprising enveloping	50	
Improvement grants	35	
Innovation		44
Enterprise		5
		159

This assumes that the extension of temporary short-time working scheme is dropped.

5. We have foreseen threats to the Reserve amounting to £735m, as in appendix 1 (unchanged from my minute of 21 February). Further bids will come forward during the year. But some of those foreseen may not materialise, or not fully, or may be judged not charges to the Reserve. (The £140m for additional overseas students grants as a result of the Court judgment needs further examination in this regard.)

6. It remains my view that up to £350m of the Reserve for 1983-84 might be committed for Budget measures, but anything over £100m must be regarded as reducing forecast shortfall and thus be scored against the fiscal adjustment. But the pressure on the Reserve is now looking quite serious. It would be much better and safer to keep the commitments from the Budget well within this figure.

7. I record here, for reference, that what is said above as to scoring against the fiscal adjustment derives from the assumption for forecasting purposes that of the £1500m Reserve, £750m will be fully spent on bids other than from the nationalised industries, and the forecasters' view that the nationalised industries will not in practice take any of the £750m earmarked for them. PE think that the amount earmarked for nationalised industries could be reduced to £500m. This releases £250m for other purposes, but it scores against forecast shortfall and hence against the fiscal adjustment. So that the other £100m shall not be scored against shortfall we have to assume it taken from the other half of the Reserve, the £750m assumed fully spent. We already have the £735m threats, and have to assume that sufficient of these disappear to leave room.

8. I record again also that the planning total for 1983-84 will also be affected by estimating changes not charged to the Reserve, but the present view is that these changes go in both directions and cancel out, making the net change insignificant.

AKR

A K RAWLINSON

Appendix 1

CONTINGENCY RESERVE 1983-84

The Contingency Reserve for 1983-84 in the White Paper is set at £1500 million.

2. Apart from the nationalised industries the main threats foreseen at present, apart from Budget measures, are:

		£ million
Industry		
(i)	Finance for BL	150
(ii)	Launch aid Various airframe and aero engine projects for which there is currently no PES provision.	50
Defence		
(iii)	Armed Forces pay To allow for possiblity of acceptance of AFPRB recommendations higher than 3½ per cent. But some underspending is possible on defence budget in 1983-84, so that an amount of this size could be absorbable unless something unexpected happens to the exchange rate or to inflation.	70
Health		
(iv)	Restoration of DDRB abatement Left on one side in PES discussion. Could be difficult to resist. Might be some offsetting savings.	45
(v)	Pharmacists' profits	10
Home Office		
(vi)	Police pay	25
(vii)	Enhanced civil defence planning.	15
Treasury		
(viii)	Indemnities to Bank of England for support to Mexico and Brazil	135
FCO		
(ix)	UK contributions to peace-keeping force in Namibia. Contingent on events. Probability may be small.	20
(x)	Overseas students fees: Agreed package Court judgment about eligibility.	5 140
(xi)	Loan to Yugoslavia	40
Public services pay		
(xii)	If increases exceed 3½% but are less than say 4½%, they should be containable, but some small departments may be in difficulty: say	10
Other		
(xiii)	Including territoral consequentials	20
	TOTAL	735

3. Some of these items may not materialise. But further threats not included above must be mentioned:

a) If public services pay increases were more than say 4½%, containment would be difficult generally. Each 1% represents about £50m.

b) Failure to hold the decision to recover the overshoot on national insurance benefits would cost £180m if the sweeteners were not conceded, £250m if the sweeteners were conceded as well.

c) Nothing is included for petrochemicals, or for energy prices.

Pup

FROM: C D HARRISON
DATE: 22 FEBRUARY 1983

PS/MINISTER OF STATE (C)

cc Principal Private Secretary
PS/Chief Secretary
PS/Financial Secretary
Mr Colman
Mr Salveson
PS/C&E

FIRST ORDER PQs, THURSDAY 24 FEBRUARY

As I told you on the telephone, the Economic Secretary has made comments on the draft replies and notes for supplementaries to questions No.1, 7 and 15. I attach, on separate sheets, his suggestions.

CDH

C D HARRISON

ECONOMIC SECRETARY TO THE TREASURY

QUESTION 1 - MR R C MITCHELL MP

The Economic Secretary has amended the draft supplementary 10 as follows:-

Q. Many charities provide services which supplement National Health Service provisions. Why cannot they be allowed a VAT refund in line with the arrangement announced last week for refund of VAT on services contracted-out by NHS hospitals?

A. The arrangement to which the hon member refers is a method of providing government support to public bodies which, unlike charities, are already paid for out of taxation. If they incurred VAT on contracted-out services it would simply add to the total size of the tax bill. There would be no sense in that. In any case, a VAT relief could not be limited to selected charities, such as those operating in the health field. Everyone has passionately held views about which charities are most deserving, and selective relief would be widely regarded as indefensible by non-beneficiaries.

This has been cleared with officials.

Question 7 - Miss Joan Lestor MP

The Economic Secretary felt that the original draft answer was much too forthcoming, since the government has no plans to give VAT relief on further items of baby care, and every reason not to do so. So he would suggest:

> "Babies' clothing and footwear are already relieved from value added tax, as is most baby food. To go beyond this would raise formidable problems of definition and repercussion. Nevertheless, the possibility of relieving other items of baby care will be borne in mind by my rt hon and learned friend in preparing his Budget."

This has been cleared with Customs.

ECONOMIC SECRETARY TO THE TREASURY

Question 15 - Mr Clement Freud MP

The Economic Secretary thinks that the following supplementary might be useful, in spite of Mr Freedman's background note 6:

Q. Is it not quite indefensible that racecourses should be faced with closure by Customs' sudden decision to charge VAT on entry fees which do not even go to them?

A. There has been no sudden decision by Customs. The Racecourse Association and the Jockey Club were advised in December 1980 that the exemption of users' entry fees from January 1981 could give rise to a reduced input tax entitlement. They have ignored that warning. /I cannot deal with the merits of the assessments. Each racecourse has the right of appeal to the independent VAT Tribunal. I understand that the Racecourse Association is going to sponsor a test case/.

[supplied by Customs]

CHANCELLOR OF THE EXCHEQUER

for PM's mtg

(1) Background for Alec mtg:

How many - out of how many - speakers asked for action on NIS? 6/21 (10/21 for industry).

(2) Can AWR give any similar idea from mtg see below No. 11 Tories?

(3) Wh has public opinion poll evidence also -
Industry 3 X % 80:20
People X %
- 1 think? - with Tories even keener.

CONFIDENTIAL

E.3

FROM: ADAM RIDLEY
23 February 1983

CHANCELLOR

CONTACTS WITH MPs: ADVOCACY OF NIS CUT AND HELP FOR INDUSTRY

The attached list records those whom the minutes of your backbench meetings record as advocating NIS cuts. As you know, these discussions cover wide ground rather selectively. So many of those supporting (or opposing) any given idea will not have spoken and been recorded, or done more than nod in agreement or shake their heads. The list shows an interesting spread across the party spectrum, with Whitney and Budgen as keen as Lester and Hicks. Compared to last year, the unprompted advocacy is less; and this year a small number of colleagues have come out explicitly against.

2. It is also worth noting that one of the notable features of your talks has been the emphasis on no gross give-aways, no electioneering, and nothing which could be criticised as vote-buying by income tax cuts. The vast majority of those present have said "hear-hear" whenever that point is made.

3. Nearly everyone who has spelt out "his" budget in full has gone for a balance between income tax and helping business and enterprise. Some say "thresholds are my no 1 priority, but I'd also like to see something significant for enterprise, business costs, etc." while some put business costs first and make thresholds the residual. This very clear pattern tells us that the Parliamentary Party would be concerned at a Budget which was at either extreme.

4. CBI influence has been much less apparent in the case of those favouring industry than it was last year. Neither they nor IOD have made many total converts, and backbenchers give every sign of speaking their own minds more than previously.

AR

A N RIDLEY

There are almost certainly no other single issues which have elicited anything approaching this amount of support other than the tax thresholds, the [illegible] & (perhaps) charities

LIST OF MPs ADVOCATING NIS CUT SINCE THE AUTUMN STATEMENT

J Lester
K Speed
R Whitney
Sir H Fraser
M Latham
N Budgen
N Thorne
R Hicks
R Banks
Sir P Mills
J Stokes

+ probably some of R Needham's group, with whom there is to be a meeting on Monday.

Backbench Finance Cttee

	Specific mention of NIS	"Help for Industry"	Nowt for industry	No comme[nt]
1.				Townend
2.		Munro "new industry"		
3.	Maxwell-Hyslop			
4.				Hordern (people)
5.			Eggar	
6.		Morrison		
7.	Miller			
8.				Bryan (peopl[e])
9.	[illegible]			Madel (CB, UB)
10.	R	Prentice		
11.				Carlisle (peopl[e])
12.	Peyton			
13		Beaumont-Dark		
14.	Cranborne (+CT)			
15.	Patten			
16.	Mills			
17.				Costain
18.				Jessel
19.				Rees-Davies
20.				Forman
21.				Morris (people)

V. pro NIS cut : 6/21
pro-industry unspecified : 4/21 = 10/21 for industry
pro-people 6/21

CONFIDENTIAL

E.3

FROM: ADAM RIDLEY
23 February 1983

CHANCELLOR

MORTGAGE INTEREST RELIEF

A recent survey on public attitudes - copy attached at Flag B - revealed fairly clearly how important the electorate hold raising the £25,000 limit in relation to other Budget priorities. Reminded that the Chancellor would have a limited sum available, and would have to choose between raising the £25,000 limit, reducing income tax, reducing business taxes, raising social security/ reducing excise duties on alcohol/tobacco/petrol, the result was ("don't knows"excluded in each comparison):

Income Tax	85
Mortgage limit	7
Business Tax	61
Mortgage limit	21
Social Security	78
Mortgage limit	14
Excise Taxes	49
Mortgage limit	39

[See page 4 of full survey report]

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When those in the sample who had current mortgages were isolated, and their replies were analysed, the breakdown was very similar.

2. This set of answers shows not only the great preference for cutting income or business tax or raising social security, but also the <u>lack</u> of general concern about increases in excise duties.

AR

A N RIDLEY

I.S.

PUBLIC ATTITUDES TO MORTGAGE INTEREST RATES

1. Introduction

The Party commissioned from Gallup some questions on attitudes to tax relief on mortgages. The interviewing for this survey was conducted from 2nd to 7th February and Gallup interviewed 930 electors throughout Great Britain. This particular survey found 43% claiming they would vote Conservative, 30% Labour, 13% Social Democrat and 11% Liberal.

2. Home Ownership

Gallup asked respondents 'Do you, or your family, own your own home or do you rent it?" They found 38% saying they are buying their home on a mortgage, 26% renting from the Council, 24% they are buying their home on a mortgage, 10% they are renting their home from a private landlord and 2% living in a hostel, lodgings etc. Details of the profile of home ownership for supporters of the main parties are shown below:-

Home Tenure	All	Conservative Supporters	Labour Supporters	Liberal Supporters	SDP Supporters	Others
	%	%	%	%	%	%
Own: Paid for	24	33	15	28	21	2
Own: Buying on Mortgage	38	42	26	38	53	32
Rent from Council	26	15	45	23	18	36
Rent privately	10	7	13	10	5	31
Hostel, lodgings etc	2	3	1	2	3	0

3. Mortgage Tax Relief

Gallup asked respondents 'Do you know that the interest payments on money borrowed under a mortgage can be 'set off' against the borrowers income tax?' They found 69% claiming to be aware that such interest payments can be 'set off' against income tax, 25% claiming not to be aware of this and 7% did not answer. Among Conservative supporters 77% claimed to be aware of tax relief on mortgage payments, among Labour supporters 57%, among Liberal supporters 63% and among SDP supporters 80%. Details are shown below:-

Aware of Existence of Mortgage Tax Relief

	All	Conservative Supporters	Labour Supporters	Liberal Supporters	SDP Supporters
	%	%	%	%	%
Yes	69	77	57	63	80
No	25	17	34	28	15
Don't Know	7	6	9	9	5

Among respondents buying their homes on a mortgage 85% claimed to be aware of home tax relief on mortgage interest payments, but among council tenants only 46%. Details are shown below:-

Aware of Existence of Mortgage Tax Relief

	All	Own Home	Buying Home on Mortgage	Rented from Council	Rented Privately
	%	%	%	%	%
Yes	69	75	85	46	53
No	25	18	12	43	38
Don't Know	7	46	2	12	9

We asked respondents 'Are you aware of any limit on the size of mortgage which qualifies for this tax relief?' 28% claimed to be aware of a limit, 62% claimed not to be aware of a limit and 9% did not have a view. Details of the answers to this question for the supporters of the main parties and for home owners and those buying their homes on a mortgage are shown below:-

Awareness of Size of Mortgage which Qualifies for Tax Relief

	All	Conservative Supporters	Labour Supporters	Liberal Supporters	SDP Supporters
	%	%	%	%	%
Yes	28	32	19	29	32
No	62	60	66	60	66
Don't Know	9	8	15	11	3

	Own Home	Buying Home on Mortgage	Rented from Council	Rented Privately
	%	%	%	%
Yes	29	42	13	15
No	62	55	70	70
Don't Know	9	3	18	14

Among respondents buying their own home on a mortgage 42% claimed to be aware of the limit to the size of mortgage which qualifies for tax relief - this compares with 29% being aware of this provision among home owners, 13% among council tenants and 15% of those in the private rented sector.

The electorate's view on whether the £25,000 limit is reasonable or not is very evenly split with 41% regarding it as reasonable, 40% as not reasonable and 19% not having a view. Details of attitudes for the supporters of the main parties are shown below:-

£25,000 Reasonable Limit for Tax Relief on Mortgages

	All	Conservative Supporters	Labour Supporters	Liberal Supporters	SDP Supporters
	%	%	%	%	%
Is reasonable	41	44	42	38	39
Is not reasonable	40	43	30	43	52
Don't Know	19	13	28	19	10

	Own Home	Buying Home on Mortgage	Rented from Council	Rented Privately
	%	%	%	%
Is reasonable	46	42	36	39
Is not reasonable	38	54	26	33
Don't Know	16	5	39	28

When Gallup asked 'Some people say that the £25,000 limit on tax relief for mortgages should be increased by the Chancellor in this budget. How important do you think it is that he should raise this limit?' 32% thought it was 'very important' that he should raise the limit, 36% 'not very important', 18% 'not at all important' and 14% did not know.

Importance of Increasing £25,000 Limit

	All	Conservative Supporters	Labour Supporters	Liberal Supporters	SDP Supporters
	%	%	%	%	%
Very Important	32	34	24	38	39
Not very important	36	39	34	32	42
Not at all important	18	17	22	12	14
Don't Know	14	10	20	17	6

Details of the answers to this question 'broken down' for various types of housing are shown below:-

	Own Home	Buying Home on Mortgage	Rented from Council	Rented privately
	%	%	%	%
Very Important	31	41	22	24
Not very important	37	41	28	36
Not at all important	19	12	23	23
Don't Know	14	6	27	17

4. Alternative to Increasing Tax Relief on Mortgages

In order to compare the relative importance of raising the level of tax relief on mortgages with other possible changes Gallup asked 'In producing his budget the Chancellor is likely to have a limited amount of money which could be used to raise the £25,000 limit on mortgage tax relief or to reduce taxes or increase benefits like social security or pensions. For each of the following which would you prefer him to use that amount of money for:-

a) Raising the £25,000 limit on mortgage tax relief or using it for reducing income tax?

b) Raising the £25,000 limit on mortgage tax relief or using it to reduce taxes on business.

c) Raising the £25,000 limit on mortgage tax relief or using it for reducing the tax on alcohol/tobacco/petrol.

d) Raising the £25,000 limit on mortgage tax relief or using it for increasing social security benefits like pensions or child benefits.

When asked about increasing the limit for mortgage tax relief or reducing income tax only 7% wanted to raise the limit and 85% favoured using money for reducing income tax.

When faced with a choice of raising the £25,000 limit or using money to reduce taxes on businesses - 21% selected raising the £25,000 limit and 61% using limited money to reduce taxes on business.

When faced with a choice of raising limit on mortgage tax relief or reducing tax on alcohol/tobacco or petrol 39% selected raising mortgage tax relief limit and 49% reducing alcohol/tobacco/petrol tax.

When faced with a choice between raising the £25,000 limit or using it to increase social security benefits 14% selected raising £25,000 limit and 78% increasing social security benefits.

Details of the answers to this question for supporters of the main parties are shown below:-

In producing his Budget the Chancellor is likely to have a limited amount of money which could be used to raise the £25,000 limit on mortgage tax relief or to reduce taxes or increase benefits like social security and pensions. For each of the following which would you prefer him to use that amount of money for:

Voting Intention

	Total	Conservative Supporters	Labour Supporters	Liberal Supporters	SDP Supporters
	%	%	%	%	%
Raising the £25,000 limit on mortgage tax relief	7	7	5	7	10
Using it for reducing income tax	85	87	83	84	84
Don't Know	8	6	12	9	6
Raising the £25,000 limit on mortgage tax relief	21	17	22	27	22
Using it for reducing taxes on business	61	70	54	60	64
Don't Know	17	13	24	13	13
Raising the £25,000 limit on mortgage tax relief	39	46	27	50	45
Using it for reducing the tax on alcohol/tobacco/petrol	49	43	57	37	49
Don't Know	12	11	16	13	6
Raising the £25,000 limit on mortgage tax relief	14	20	6	17	13
Using it for increasing social security benefits like pensions or child benefits	78	72	84	77	80
Don't Know	8	8	11	6	7

5. Labour and the Economy

We asked respondents whether they thought a Labour victory at the General Election would be good for growth and jobs, inflation and unemployment. Gallup found 39% thought a Labour Government would be good for growth and jobs, 42% bad and 19% did not have a view. 19% thought a Labour government would be good for inflation, 60% bad for inflation and 21% did not have a view. 51% thought a Labour government would be good for unemployment, 31% bad and 19% did not have a view.

Details of the analysis of this question for supporters of the main parties is shown below:-

If the Labour Party wins the next election do you think their economic policy would be good or bad for:-

	All	Conservative Supporters	Labour Supporters	Liberal Supporters	Alliance Supporters
	%	%	%	%	%
(a) Growth and Jobs					
Good	39	13	79	38	46
Bad	42	73	6	35	38
Don't Know	19	14	15	27	16
(b) Inflation					
Good	19	3	46	21	19
Bad	60	86	30	57	62
Don't Know	21	11	25	22	19
(c) Unemployment					
Good	51	28	85	46	66
Bad	31	51	5	36	23
Don't Know	19	22	11	18	11

When Gallup asked 'Some people say that if Labour win the next election this could plunge the country into an economic crisis. Do you think this is true or not?' 45% thought this is true, 40% not true and 14% did not have a view.

Details of the analysis for this question is shown below:-

Labour victory in General Election plunge country into economic crisis

	All	Conservative Supporters	Labour Supporters	Liberal Supporters	Alliance Supporters
	%	%	%	%	%
True	45	77	7	45	39
Not true	40	13	77	43	50
Don't Know	14	10	16	12	11.

8.2.83

CONFIDENTIAL

E.3

FROM: ADAM RIDLEY
23 February

CHANCELLOR

BUDGET: OPINION RESEARCH

EVIDENCE ON PRIORITIES

In our recent survey on interest rates, exchange rates etc., the question we included on priorities and the choice between wage earners and industry showed a majority of nearly five to one in favour of helping industry, with Conservative supporters keenest of all (87 to 9 in favour). The full result is at Flag A in the attached report.

AR

A N RIDLEY

Public Attitudes to Interest Rates and Exchange Rates

1. Introduction

We have just received the results of the questions on public attitudes to interest rates and exchange rates that we commissioned from Gallup. Gallup conducted the survey from 27th to 31st January and interviewed almost 1,000 electors. The survey also included a voting intention question which found 45% claiming they would vote Conservative, 31% Labour; 10% Liberal, 12% Social Democrat and 2% for 'other' parties.

2. Interest Rates

Gallup asked 'In recent months there has been a lot of talk in the press and on TV about interest rates. Would you say that over the last year or so they had gone up, gone down or stayed the same.' 17% thought they had gone up, 53% they had gone down, 16% stayed the same and 14% did not answer.

Details of the analysis of the results for supporters of the main parties and for the main socio-economic groups in the electorate are shown below:-

Interest Rates Up/Down

	All	Conservative Supporters	Labour Supporters	Liberal Supporters	Alliance Supporters
	%	%	%	%	%
Gone up	17	12	23	21	14
Gone down	53	61	44	47	63
Stayed the same	16	15	19	24	12
Don't Know	14	12	15	9	11

Age

	Men	Women	18-34	35-44	45-64	65+
	%	%	%	%	%	%
Gone up	16	18	14	14	22	16
Gone down	59	47	54	63	52	41
Stayed the same	15	18	15	15	18	18
Don't Know	10	18	17	8	8	25

	Class			House Ownership		
	ABC'1	C2	DE	Own Home	Buying on Mortgage	Council Rented
	%	%	%	%	%	%
Gone up	10	21	20	17	11	23
Gone down	64	53	37	53	68	37
Stayed the same	17	15	18	17	13	18
Don't Know	9	11	25	13	8	21

Among Conservative supporters 12% thought interest rates had gone up, 61% gone down, 15% stayed the same and 12% did not know. Among Labour supporters 23% thought interest rates had gone up, 44% gone down, 19% stayed the same and 15% did not know. 21% of Liberal supporters thought interest rates had gone up, 47% gone down, 24% stayed the same and 9% did not know. 14% of Alliance supporters thought interest rates had gone up, 63% gone down, 12% stayed the same and 11% did not know.

Women are more likely than men to not know what has happened to interest rates. Men are more likely than women to think that interest rates have gone down. Looking at attitudes among the various age groups those in the 45-64 age group are more likely to be aware of the increase in interest rates. In class terms 10% of the ABC1 group thought interest rates had gone up, 64% gone down and 17% stayed the same. Among the C2 group 21% thought they had gone up, 53% gone down and 15% stayed the same. Looking at attitudes among electors buying their homes on a mortgage 11% thought interest rates had gone up, 68% gone down and 13% stayed the same.

We asked respondents 'Do you think it matters much for the economy and business when interest rates go up? 67% thought it matters a lot, 13% matters a little, 9% that it does not make any difference and 11% had no view. Details of the analysis of this question for the supporters of the main parties is shown below:

Interest Rates Matter Much for the Economy and Business

	All	Conservative Supporters	Labour Supporters	Liberal Supporters	Alliance Supporters
	%	%	%	%	%
Matters a lot	67	72	63	57	77
Matters a little	13	12	14	17	8
Does not make any difference	9	7	11	12	2
No view	11	8	12	15	12

72% of Conservative supporters agreed with the view that it matters a lot for the economy and business when interest rates go up. 63% of Labour supporters took the same view, as did 57% of Liberal supporters and 77% of Alliance supporters.

3. Ex[illegible]nge Rates

Gallup asked respondents 'Would you say the foreign exchange rate for the pound - that is what the pound is worth in terms of foreign currencies - has risen or fallen since last summer?' 11% thought exchange rates have risen, 71% fallen and 18% did not have a view. Details of the analysis of this question for the main parties is shown below:-

Foreign Exchange Risen/Fallen

	All	Conservative Supporters	Labour Supporters	Liberal Supporters	Alliance Supporters
	%	%	%	%	%
Risen	11	13	12	17	4
Fallen	71	70	72	67	81
Don't Know	18	17	16	16	16

On the question of floating exchange rates Gallup asked 'At present the exchange rate between the pound and foreign currencies changes freely from day to day. Do you think that the Government should try and hold it steady or should it continue to allow it to vary?' 50% thought the Government should try and hold the exchange rate steady, 33% allow it to vary and 17% did not have a view. Details of the analysis of this question for the main parties is shown below:-

Exchange Rate Hold Steady/Allow to Vary

	All	Conservative Supporters	Labour Supporters	Liberal Supporters	Alliance Suporters
	%	%	%	%	%
Hold Steady	50	37	63	63	54
Allow to Vary	33	46	19	25	25
Don't Know	17	17	18	12	12

Among Conservative supporters 37% thought the Government should hold the exchange rate steady, 63% of Labour supporters took the same view as did 63% of Liberal supporters and 54% of Alliance supporters. 46% of Conservative supporters thought the exchange rate should be allowed to vary, as did 19% of Labour supporters, 25% of Liberal supporters and 25% of Alliance supporters.

With regard to the effect of the exchange rate on individuals we asked 'Some people say that changes in the exchange rate for the pound does not matter very much? (a) When the exchange rate falls does this worry you personally? (b) How about when the exchange rate improves, does this worry you personally?' 34% regarded the fall in the exchange rate as worrying for them personally, 59% that it is not and 7% did not have a view. On the question of improvement in the exchange rate 10% of respondents regarded this as worrying, 82% as not worrying and 7% did not have a view.

When Gallup asked 'Do you think that a fall in the rate of exchange for the pound is on balance a good thing or a bad thing for the country?' 17% thought a fall in the exchange rate is a good thing, 57% a bad thing and 26% did not have a view.

On the question of Britain's image in the world we asked 'Do you think that a fall in the rate of exchange does or does not affect Britain's image in the world?' 74% thought that it does, 13% that it does not and 13% did not have a view.

When asked about what the Government should do if the value of the pound starts to fall again opinion was fairly evenly divided. Gallup found 39% thought the Government should let interest rates go up, 39% not let interest rates go up and 23% did not have a view. On the question of the Government being prepared to introduce a less generous budget in order to maintain the value of the pound - 44% thought it should be prepared to introduce a less generous budget, 35% not introduce a less generous budget and 21% did not have a view.

Details of the answers to these questions analysed by supporters of the main parties is shown below:-

Should the Government try to hold the value of the pound if it starts to fall again? In particular, should the Government be prepared to:

(a) Let interest rates go up?

	All	Conservative Supporters	Labour Supporters	Liberal Supporters	Alliance Supporters
	%	%	%	%	%
Yes	39	40	38	46	38
No	39	40	39	33	34
Don't Know	23	20	22	20	28

(b) Introduce a less generous budget?

	All	Conservative Supporters	Labour Supporters	Liberal Supporters	Alliance Supporters
Yes	44	49	40	46	48
No	35	33	37	32	33
Don't Know	21	18	22	22	19.

4. Help for Industry

When Gallup asked 'If the Government has only a limited amount of money that can be used to help wage earners or to help strengthen industry which should it do?' Support for helping industry was very high among all groups. In the electorate 16% thought the Government should help wage earners, 76% help strengthen industry and 8% did not have a view. An analysis of support for the main parties is shown below:-

Money for Wage Earners or Help Strengthen Industry

	All	Conservative Supporters	Labour Supporters	Liberal Supporters	Alliance Supporters
	%	%	%	%	%
Help wage earners	16	9	23	18	12
Help strengthen industry	76	87	67	67	83
Don't Know	8	5	10	10	5

5. Labour and the Economy

We asked respondents whether they thought a Labour victory at the General Election would be good for growth and jobs, inflation and unemployment. Gallup found 39% thought a Labour Government would be good for growth and jobs, 42% bad and 19% did not have a view. 19% thought a Labour government would be good for inflation, 60% bad for inflation and 21% did not have a view. 51% thought a Labour government would be good for unemployment, 31% bad and 19% did not have a view.

Details of the analysis of this question for supporters of the main parties is shown below:-

If the Labour Party wins the next election do you think their economic policy would be good or bad for:-

	All	Conservative Supporters	Labour Supporters	Liberal Supporters	Alliance Supporters
	%	%	%	%	%
(a) Growth and Jobs					
Good	39	13	79	38	46
Bad	42	73	6	35	38
Don't Know	19	14	15	27	16
(b) Inflation					
Good	19	3	46	21	19
Bad	60	86	30	57	62
Don't Know	21	11	25	22	19
(c) Unemployment					
Good	51	28	85	46	66
Bad	31	51	5	36	23
Don't Know	19	22	11	18	11

When Gallup asked 'Some people say that if Labour win the next election this could plunge the country into an economic crisis. Do you think this is true or not?' 45% thought this is true, 40% not true and 14% did not have a view.

Details of the analysis for this question is shown below:-

Labour victory in General Election plunge country into economic crisis

	All	Conservative Supporters	Labour Supporters	Liberal Supporters	Alliance Supporters
	%	%	%	%	%
True	45	77	7	45	39
Not true	40	13	77	43	50
Don't Know	14	10	16	12	11.

8.2.83

cc CST
FST
EST
MST(C)
MST(R)
Mr Middleton
Mr Moore
Mr Robson
Mr Ridley
Mr French
Mr Harris
PS/IR

Treasury Chambers, Parliament Street, SWIP 3AG
01-233 3000

23 February 1983

The Rt. Hon. Sir Keith Joseph Bt MP
Secretary of State for Education and Science

Dear Keith

HOUSE OF LORDS DECISION - WICKS V FIRTH, JOHNSON V FIRTH

EMPLOYER SCHOLARSHIPS

You are already aware of this House of Lords decision, given on 16 December last.

The case concerns scholarships provided through an educational trust set up and financed by ICI for the children of its employees. The House of Lords was asked to decide whether the value of the scholarships received by the students were taxable as fringe benefits of the parents. For the Revenue it was argued that, while Section 375 of the 1970 Taxes Act applied to exempt the scholarships from tax in the hands of the scholars, the exemption did not apply to such benefits when they came effectively to the parents because of their employment by ICI. This argument was accepted by a majority in the Court of Appeal. The House of Lords, however - also by a majority - decided that while the scholarships were undoubtedly fringe benefits of the parents, Section 375 extended to exempt them in the parents' hands.

I have considered whether we could simply live with the Lords' decision on the grounds that schemes of this kind are a means of indirectly attracting, albeit upon a selective basis that was essentially dependent upon the parents' employment, additional financial resources to education. However, I have concluded that this would be wrong, and in the last resort indefensible. Employers' scholarships of this kind are indistinguishable from any other "fringe benefit". Like many other such benefits, they came into existence (as I know from my own experience with one company) as a means of mitigating the high marginal tax rates which we got rid of in 1979. To leave them with a special tax advantage would be widely seen as unfair - and inconsistent with what we ourselves have often said about the "perks" society.

Morever, while the tax loss would currently probably be no more than £m10 a year, that figure could be expected to grow rapidly if no action were taken. After all, schemes do not only provide scholarships for undergraduates but some cover everything from preparatory school to doctorates. And already Press articles are suggesting that companies should take advantage of the situation created by the House of Lords' decision in Wicks v Firth on the basis that there is little to lose if the Government did legislate.

I felt it right to tell you that I propose to introduce in this year's Finance Bill a provision designed to bring into charge on the parents the benefit of scholarships which come to students because of their parents' employment. The charge will apply to payments made for the academic year 1983/84 and later years - payments for earlier periods will be exempt in accordance with the House of Lords' decision. Employers will naturally still get a tax deduction for the money they spend on these schemes. This is right and fair because the costs are part of the remuneration package they offer to their employees along with salary, pension rights and company car.

There is of course no question of taxing genuinely charitable scholarships won in open competition; these will remain tax free for scholars and parents alike. The intention of Section 375 would thus continue to be fulfilled. This was originally enacted in 1920 in order to exempt scholarship income from tax in the hands of the person being taught, and that purpose is as desirable today as it was (rightly) thought to be in 1920.

As you will imagine, I did not arrive at this decision lightly. In particular I have been conscious of the need to avoid causing possible hardship to those parents who are currently enjoying the value of scholarships which will now give rise to taxable benefits. But I think it is true to say that all those affected will have recognised and accepted at least the possibility of taxation when the scholarship first became payable. In any event I hope that the period of grace to the end of this academic year will give them time to appraise the changed situation and make any dispositions that are necessary.

For the record, I should point out that we are <u>not</u> concerned with school fees etc paid by employers when the parents are abroad on business. These are and will continue to be covered by quite separate categories of relief which in different forms provide special treatment for service overseas of employees in both the public and the private sectors.

Likewise, the same tax rules apply to Crown servants and others who continue to draw boarding school allowance while serving in the United Kingdom. In such cases boarding school allowances paid are fully taxable as an addition to remuneration. In short, we are not vulnerable to criticism that by bringing scholarship schemes like ICI's into tax we are taxing the private sector while tolerating an anomaly in the public sector - on the contrary we are acting to maintain consistency of tax treatment.

I realise the difficulties of this course of action, with an election not far away; and some of our supporters will be disappointed by what I propose. But to leave this unintended tax advantage in place would be to allow a relatively small number of people, whose remuneration was arranged in a particular way, to achieve help with their school fees by the "back door". Many people who are not offered similar facilities by their private sector employers, and all in the public sector, would not be able to benefit from this. If we want to provide tax relief for private education, we should decide to do it for all as a matter of deliberate policy. I am sure it would be wrong to do so simply by turning a blind eye to the consequences of a decision in the House of Lords.

One final and not unimportant point. I am considering for my Budget on 15 March a number of measures which will include significant benefit to those with larger incomes and capital. I am firmly convinced that measures of this kind (even when they are placed alongside the other similar reliefs that we have already introduced) are fully justified. But we must be prepared to rebut the inevitable criticism from our opponents. And to do this convincingly, we must be able to show that we are equally firm when arrangements of the kind which we are now discussing confer an unfair advantage.

I am copying this letter to the Prime Minister.

GEOFFREY HOWE

CONFIDENTIAL

MTFS Box

FROM: RACHEL LOMAX
DATE: 23 FEBRUARY 1983

CHANCELLOR

cc: Chief Secretary
Economic Secretary
Sir D Wass
Sir A Rawlinson
Mr Burns
Mr Middleton
Mr Littler
Mr Cassell
Mr Evans
Mr Odling-Smee
Mr Mountfield
Mr Kemp
Mr Ridley
Prof. Walters

See scribbles on text

All seen by Mrs Lomax.

MEDIUM TERM FINANCIAL STRATEGY

You wanted to look at the MTFS alongside the draft section of the FSBR on the short term forecast. I attach a further draft which takes account of comments made at your last meeting and received subsequently from the Bank. Mr Evans is putting forward a separate note on the relationship between the forecasts for the RPI and GDP deflator.

Coming minute on LAF

R. Lomax

pp RACHEL LOMAX

MEDIUM TERM FINANCIAL STRATEGY - DRAFT

1. Government policies have helped to bring about a rate of inflation that is already well into single figures. The objective over the medium term is to continue reducing inflation, and to secure a lasting improvement in the performance of the UK economy, so providing the foundations for sustainable growth in output and employment. Firm financial policies are an essential means to this end. The medium term financial strategy sets out the framework within which policy is operated.

2. Control of the money supply is a central part of this strategy. In judging the rate of monetary growth needed to reduce inflation, the Government will continue to take account of structural influences on the different monetary aggregates, as well as the behaviour of other financial indicators. Fiscal policy is designed to be consistent with this monetary framework and with the overall objective of reducing inflation. Over a period of years, a reduction in public sector borrowing, as a proportion of GDP, has a key part to play in securing a fall in interest rates, in both real and nominal terms.

3. The extent of the recovery in real activity over the next few years depends critically on bringing down cost increases, in all sectors of the economy. Lower domestic costs will enable British industry to compete more effectively, at home and abroad, without adding to inflationary pressures. Despite recent gains, UK productivity is still low in comparison with other major industrial countries. The long term health of the economy depends on further efforts to close this gap. Moderation in pay will help to ensure that improved efficiency is reflected in higher output and employment.

4. The Government will continue to pursue policies to strengthen the supply performance of the economy, by providing greater incentives for work and enterprise, and by improving the working of markets. A low rate of inflation will provide the right macro-economic environment in which these policies can succeed.

Recent Financial Conditions

5. Monetary conditions have developed broadly as intended over the past year; in the year to February, the growth of the key monetary aggregates was within the target range of 8-12 per cent. Combined with the rapid fall in inflation, this contributed to a substantial fall in interest rates. By mid-November, short term rates had come down to 9 per cent but, as the exchange rate weakened, market rates, and with them base rates, rose to around 11 per cent. In recent weeks however short term interest rates have fallen back to around [ ] per cent.

Table 2

MONETARY GROWTH 1982-83

Percentage growth

	M_o(1)	M1	M2	£M3	PSL1	PSL2
February 1982-February 1982	[3½]	[11½]	[6]	[10]	[9]	[8½]

(1)Monetary base, wide definition

6. £M3 grew by 10 per cent over the first twelve months of the target period. During the spring and early summer the rate of growth was close to the bottom of the range. There was some rise in the late summer and autumn, but since November growth has again slowed down. PSL2 grew by less thn £M3 - [8½] per cent in the year to February - in part reflecting the fact that a large proportion of building societies' inflows were into term shares which are not included in PSL2. Although such shares have become more liquid in recent years, as facilities for early withdrawal have been offered, there is generally still a significant penalty for early access in the form of a period of notice and loss of interest. The growth of bank lending followed much the same profile as that of £M3. This in-year variation was attributable largely to borrowing by companies, borrowing by persons remaining high throughout the year.

7. M1 grew more slowly than £M3 over the period 1979-81. Last year, as expected, M1 responded to the fall in interest rates and its growth rate rose, to finish at [11½] per cent over the twelve months to February. Narrower measures of money, including the new monetary aggregate M2, continued to grow comparatively slowly. The monetary base grew by only [3½] per cent, despite lower interest rates, possibly reflecting a faster trend decline in the importance of notes and coins relative to other means of payment.

8. Other financial indicators pointed to moderately restrictive monetary conditions. As in other industrial countries real short term interest rates remained high. While the prices of some financial assets rose strongly, the increase in real asset prices was modest. After falling for the past two years, house prices showed some tendency to rise towards the end of the year. For most of the year the exchange rate was strong. The fall after October could be taken to suggest that conditions were becoming less restrictive, though it seems to have owed much to external factors, such as concern about oil prices and sharp movements in other currencies and, possibly, to political uncertainties.

9. Against this background, the growth in real money balances, on most measures of money, largely reflects the fall in inflation and points to a recovery in real activity. For a given growth in the nominal money supply, higher real money balances are an important mechanism by which lower inflation can help to raise the level of activity.

Monetary Policy

10. In recent years the economic significance of the wider aggregates has been affected by changes in savings behaviour and by structural changes to the financial system, associated in part with the ending of direct controls. Inflation has fallen fast despite the overrun in previous years' monetary targets. These developments led to last year's decision to raise the monetary ranges. Monetary growth within the new target range set for 1982-83 has been consistent with maintaining a reasonably restrictive stance.

11. As announced in the Budget Speech, the target range for 1983-84 is to be set at the 7-11 per cent indicated in last year's Financial Statement. As usual, this range applies to the annual rate over the fourteen months beginning in February 1983. A sustained reduction in monetary growth over a period of years will be needed to keep inflation on a downward trend. Illustrative ranges for the next few years are shown in table 3. Precise targets for 1984-85 and 1985-86 will be decided nearer the time.

Table 3

RANGES FOR MONETARY GROWTH[1]

	1983-84	1984-85	1985-86
Percentage change during year	7-11	6-10	5-9

[1] From 1983-84 onwards, the definition of £M3 will be changed to exclude public sector deposits. This is in line with the revised difinition of the PSBR (see footnote to table 6 and Part V).

12. The path shown in table 3 applies to both broad and narrow measures of money: M1 and £M3 (and PSL2). However, as noted in the last year's FSBR, the combination of lower interest rates and lower inflation is likely to lead to a period of more rapid growth in M1 than in broader measures of money. The size and timing of these effects is uncertain, but if interest rates maintain [resume] their downward path, and other indicators suggest that

Not as active a problem as this?

conditions remain moderately restrictive, it may be appropriate to allow M1 to grow more rapidly than the target range for 1983-84.

13. As explained in last years Financial Statement, the interpretation of monetary conditions will continue to take account of all the available evidence, including the exchange rate, structural changes in financial markets, savings behaviour, and movements in relative and real interest rates. However, these factors cannot be taken into account in setting monetary targets in advance. The ranges shown in Table 3 have once again been constructed on the assumption that there is no major change in the exchange rate from year to year.

Fiscal Policy

14. Sustained progress on both inflation and interest rates requires continued fiscal restraint. During the 1950's and 1960's the PSBR averaged about 2½ per cent of GNP. As Chart [ ] shows, there was a strong rise in this ratio during the first half of the 1970's, peaking in 1975-76, when the PSBR reached nearly 10 per cent of GDP. High fiscal deficits over this period were associated with high inflation and interest rates.

15. Government policies have been directed at achieving a progressive reduction in public sector borrowing over the medium term. The path that has been followed has also taken account of the depth of the recession. Two years ago the PSBR path was raised substantially for this reason, though the generally declining profile was retained. The PSBR was reduced from [5 per cent] of GDP in 1979-80 to [3½ per cent] (£8.7 billion) in 1981-82.

16. The estimated outturn for 1982-83 is [£7½ billion] equivalent to about [2¾ per cent] of GDP. This is some [£1½ billion] lower than the Autumn Statement forecast, and about [£2 billion] lower than expected at the time of the Budget, though still some way above the 2¼ per cent figure envisaged for the year now ending in the 1980 FSBR. Identifiable factors contributing to the lower outturn this year include MAINLY unexpectedly high receipts from North Sea oil taxes, reflecting a higher sterling oil price, and underspending in some areas of public expenditure, notably local authority capital. The balance consists of [illegible]

+ outturn?

17. The PSBR for 1983-84 is forecast to be [£8 billion], equivalent to about 2¾ per cent of GDP, as suggested a year ago and in the Autumn Statement. The fiscal projections summarised in table 6 show a further reduction in the PSBR as a proportion of GDP, to around [2¼] per cent in 1984-85, and [1¾] per cent in 1985-86. This path should leave room for a fall in interest rates, within the monetary guidelines, over the next few years. The

figures for 1984-85 and 1985-86 are illustrative. Decisions about the appropriate size of the PSBR in any particular year will be taken nearer the time.

18. The fiscal projections in tables 4-6 are based on the public expenditure plans shown in the Public Expenditure White Paper (Cmnd 8789), updated where necessary to take account of Budget changes and estimating changes. Further details for 1982-83 and 1983-84 are given in Part V, tables [ ]. Real output is assumed to grow by 2½ per cent a year on average over the period. The general rate of inflation, as measured by the GDP deflator was 7 per cent in 1982-83. It is forecast to fall to [5½] per cent in 1983-84. (The relationship between this forecast for the GDP deflator and the more widely known Retail Prices Index is discussed in Part 3). In the later years, inflation is assumed to be 5½ per cent in 1984-85, and 5 per cent in 1985-86. The implications of these assumptions for the growth in money GDP are shown in table 6.

GDP deflator or RPI?

Public Expenditure

19. The Public Expenditure White Paper implies an increase in the planning total of about [5 per cent] in 1983-84 and each of the two later years, [and a fall in public expenditure as a proportion of GDP from [ ] in 1982-83 to [ ] in 1983-84 and [ ] in 1985-86, given the assumed growth of money GDP]. Table 4 shows the relationship between the planning total for public expenditure and general government expenditure in national accounts terms (the definition of public expenditure lying behind the general government borrowing requirement).

Table 4: General Government Expenditure

£ billion, cash

	1981-82	1982-83	1983-84	1984-85	1985-86
Public expenditure planning total[1]					
Planning total adjustments[2]					
General government expenditure.					
Special sale of assets					
Differences due to policy measures and economic assumptions[3]					
National accounts adjustment[4]					
Interest payments					
Total expenditure in national accounts terms					

Revenue

20. The growth of Government revenues in cash terms over the medium term will depend on the growth of incomes, spending and prices, as well as policy decisions. Revenue is projected on the conventional assumption of constant indexed tax rates and allowances at the proposed 1983-84 levels. National Insurance contribution rates in future years are assumed to be adjusted to maintain the present balance of income over expenditure in the Fund. [Projections of North Sea tax revenues assume that the North Sea fiscal regime is changed as proposed in the Budget and that oil prices remain around their present levels for the next two yers and then [rise] broadly in line with world inflation.] cash/real?

[move?]

21. On these assumptions, general government receipts are projected to rise by [ ] between 1982-83 and 1984-85 (closely in line with the growth in total money incomes]. Government revenues from the North Sea may [fall slightly as a proportion of general government tax receipts, from around [ ] in 1982-83 to about [ ] . . . . .].

Table 5: General Government Receipts

£ billion, cash

	1981-82	1982-83	1983-84	1984-85	1985-86
Taxes on incomes expenditure and capital					
National Insurance and other contributions					
Interest and other receipts					
Accruals adjustment					
Total					
of which North Sea tax[1]					

[1][Royalties, Supplementary Petroleum Duty (in 1981-82). Petroleum Revenue Tax (including advance payments from 1983-84) and Corporation Tax from North Sea oil and gas production (before Advance Corporation Tax set off).]

Public Sector Borrowing

22. The new projections of Government receipts and expenditure are brought together in table 6 to provide projections of the general government borrowing requirement (GGBR) and the PSBR. The size of the fiscal adjustment [conventionally assumed to take the form of lower personal taxes] depends critically on the estimates of revenues and expenditure. These are subject to major uncertainties about, for example, the tax yield for an assumed set of tax rates, the behaviour of oil prices, and the actual level of public spending in relation to the plans.

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Table 6S Public Sector Borrowing

£ billion, cash

	1981-82	1982-83	1983-84	1984-85	1985-86
General government expenditure					
General government receipts					
Implied fiscal adjustment[1]					
GGBR					
PSBR[2]	8.7	7½	8		
as % GDP	3½	2¾	2¾	2¼	1¾
Money GDP at market prices	254	274			

[1] + means lower taxes or higher expenditure than assumed in lines 1 and 2.

[2] From 1983-84 onwards, the definition of the PSBR and its components will be altered to exclude changes in pubic sector deposits. Other minor changes will also be made (see also footnote page).

Table 7: Revenue and Expenditure: Comparison with the 1982 Projections

£ million cash

Changes (+ increases)	1982-83	1983-84	1984-85
General government expenditure			
General government receipts			
Implied fiscal adjustment(1)			
GGBR			
PSBR			

(1) By definition the fiscal adjustment for 1983-84, in this year's projections, is eliminated by the 1983 Budget measures.

23. The level of money GDP in 1982-83 is estimated to have been 2 per cent lower than expected a year ago, reflecting both lower output and lower prices. The average growth in real output from now on is much the same as in last year's projections, while the growth in prices is rather lower. [References to oil prices?] ? The main factors affecting the outturn for 1982-83 are discussed in [Part V]. Changes to expenditure in 1983-84 and 1984-85

follow the decisions set out in Cmnd 8789, and in the Budget Speech. General government receipts are now projected at the proposed 1983-84 tax rates, which are lower than those used last year. [Details]. Two projected PSBR is [little changed as a percentage of GDP, the changes to the cash figures reflecting the lower level of money GDP now forecast]. This year's Budget measures have the usual effect of taking up some of the fiscal adjustment in 1984-85.

Conclusions

24. The projections shown in tables 4-6 are no more than illustrative of one particular evolution of the economy. If the domestic and world economies develop in a different way, the projections for public finances could be substantially affected. The policy response to such changes would depend on their nature, but the intention would be to hold firmly to the strategy, by maintaining monetary conditions consistent with a continued trend to lower inflation. The key to sustained recovery lies in reducing the growth of costs and increasing the returns to investment and enterprise. Within the financial framework set out here, this would make room for a faster growth in output, without damaging the outlook for inflation.

[25. Progress in reducing inflation over the next couple of years will depend, to some extent, on the strength of the cyclical recovery in output, both domestically and in the rest of the world. The strategy outlined here presuppose a slow recovery in output and trade in other industrial countries. As explained in Part 3, the path of the Retail Prices Index over the next year or so is likely to be influenced by special factors, including the recent decline in the exchange rate, and the effect of lower mortgage interest rates. It is not to be expected, therefore, that the path of inflation will be smooth. But the Government's policies will continue to be directed towards achieving a progressive reduction in its underlying trend].

M

Ken

Will you handle x when the note comes? Could you tell George about it? — he'd be happy to arrange it, I'd thought.

M.

NOTE FOR THE RECORD

MEETING HELD AT 3 pm ON 24 FEBRUARY IN ROOM 43/SG TO DISCUSS THE PREPARATIONS FOR THE 1983 BUDGET

Present:	Mr Chambers	(Chairman)
	Mr Page	
	Mr Monaghan	
	Mr Corcoran	
	Mr Uden	
	Mr Batchelor	
	Mr Johnson	
	Mr Bobsin	
	Mrs Budgen	
	Mr Collins	
	Mr Brazier	
	Mr Ludlow	
	Mrs Marsden	
	Mrs McGill	
	Miss C. Saunders	
	Mr Carpenter	(Secretary)

Opening the meeting the Chairman stressed that in the run-up to the Budget the critical factor was time. Budget material should be finalised and made available to the WPU/CRU as early as possible. Any significant delays in finalising material would cause serious practical difficulties for the supporting services in their endeavours to meet the Budget deadlines. This was particularly true of the Budget brief. EB must chase divisions hard to ensure that they did not hold on to the text unduly in order to make cosmetic changes as opposed to change of substance. If delays were likely to occur Mr Batchelor should be informed immediately. Mr Collins confirmed that EB would do their best to secure the early finalisation of the Budget brief.

In discussion the following additional points were made:

1. Mr Batchelor agreed to liaise with Mr Page and Mr Monaghan about the numbers of Budget documents required by IDT's "clients" in general and the Lobby in particular. The Chairman said that efforts should be made to keep the overall numbers the same or to reduce them.

2. Mr Corcoran confirmed that the arrangements for securing the early delivery of other Department's Press Notices were in hand. Mr Batchelor said that he would be in touch with Mr Corcoran and IDT about the total numbers required for Press Notices this year.

3. Mr Collins confirmed that EB would require the WPU to be on standby for the Budget brief from Monday 7 March onwards. It could be assumed that the brief would be the same length as in 1982; that the same number of copies would be required and the same number of drafts (1 Midweek; 1 Friday and 1 Final). EB would chase divisions for the briefing but it was probable that there would be some slack periods when no work was immediately available to the WPU. The weekly economic brief would be required both for the week before the Budget and for Budget week (the latter would involve a lot less work than the "normal" weekly brief). Mr Batchelor said that he would need a document from EB prior to 7 March setting out in some detail the likely timing for the Budget brief and the requirements on the WPU in the run-up to the Budget (in particular whether the girls might be required to do overtime). Mrs Saunders said that the WPU girls would be quite happy to undertake whatever overtime was required during the Budget period.

4. CU and EB agreed that their existing typing support would be adequate to cope with the extra demands, as long as an extra typist was provided for Mr Macrae. Mr Batchelor would be informed in good time if there was likely to be a requirement for a typist over the Budget weekend. Mr Uden said that he had provisionally allocated Mr Macrae's typist to Room 47/2; he would investigate if a closer room might be available.

5. Mr Corcoran confirmed that arrangements for the production of the FSBR were well in hand; the cover was now being produced. At present no troubles from the printers were expected. A number of extra recipients had been added to the 1982 Budget list when the Autumn Statement was issued; he agreed to liaise with Mr Batchelor about revised total requirements.

6. On the Budget Speech, Mr Batchelor said that this was typed on the Chancellor Office's machines because the WPU's print was too small. The Chairman reiterated the need for the final version to be made available for copying by the CRU at 11 am Budget morning at the latest.

7. Mr Brazier said that the Budget Aide Memoire had been finalised, apart from any revisions to the figures which might be agreed between Mr Batchelor and IDT.

8. Mrs McGill confirmed that sufficient CRU staff would be available for the Budget weekend and the Monday night. Mr Batchelor said that the aim should be to get the Treasury Press Notices finished over the weekend (the current deadline for these was Thursday pm which would enable rolling to take place on Friday and the Budget weekend). He had arranged standby facilities (and for prior servicing) for all the CRU and WPU equipment. He would also arrange a standby for CU's electronic typewriter. Recently problems had developed with the power packs for the WPUs 860s; he would endeavour to resolve this as soon as possible. Mrs Saunders asked whether the WPU would be expected to provide back up if EB's electronic typewriter was unable to cope with the volume of Budget work. Mrs Marsden said that this would not be necessary; if problems did develop in EB/CU she would arrange for other Xerox 850 operators in the Department to act as back-up.

9. Mrs Budgen said that all the Committee Section staff would be available on the Monday night and early Budget morning; she doubted whether extra clerical help would be necessary. Mr Ludlow confirmed that he would provide any extra cupboards which might prove necessary once the totals for Press Notices had been finalised.

10. Mr Ludlow confirmed that 4 messengers would be made available to IDT at 2.30 pm on Budget Day, 2 for duty in the Press Office and 2 for carrying Budget material over to the

House from the CRU; for the latter, arrangements would be made to secure the use of a van. Mr Page agreed to provide a note in advance outlining the timing of the arrangements required by IDT.

11. Mr Monahan confirmed that the usual IDT note to Mr Uden about arrangements for telephone links etc for the media would be issued shortly. If some agencies eg BBC Radio did not require special telephone links, this was their decision and none should be provided.

12. Mr Bobsin confirmed that he would make the usual security arrangements for the Budget exercise, including the provision of Guards at No 11 Downing Street.

13. Mr Johnson (who had replaced Mr Hayden in IDT) said that he would liaise with colleagues as necessary on the collection of Press/Non-Press packages on Budget Day. The "cloakroom ticket" arrangement had not been a success and IDT would be giving further thought to alternatives. Mr Page commented that the Press had been given two opportunities by IDT to order packages; Press representatives calling without an advance order, would merely be offered a few Press Notices (non-Press callers on the same basis would receive nothing). Mr Uden confirmed he would consult the Enquiry Room about the arrangements and liaise with Mr Johnson concerning the layout of the Conference Room used as the collection point.

X 14. It was agreed that EB; CU; Chancellor's Office; WPU; CRU/EOG4 would each make their own separate arrangements with the Government Car Service for cars to take people home on Budget eve. Mr Uden confirmed that he would circulate a note on this and give the usual advance notice to the car pool. He would also make special separate arrangements for IDT's blind typist for Budget night (Tuesday) and for the WPU girl from Southend for Budget Eve.

15. Mr Monaghan agreed to provide Mr Bobsin with relevant details of the TV and Radio vehicles requiring access to the Centre Courtyard on Budget Day.

16. It was agreed that EB; CU; Chancellor's Office; WPU; CRU and EOG4 would each make their own separate arrangements for meals on Budget Eve (there would be no central "Fish and Chips" facility this year).

41

17. Mr Batchelor confirmed that he would arrange for COI to visit the Treasury to discuss their proposed use of the telex facilities in Room 35/G; he would also prepare in due course a draft Office Notice placing the CRU "out of bounds".

Circulated to: Those present
Mr Salveson
Miss Roach

Office Services Division
2 March 1983

CONFIDENTIAL

JH 13

DEPARTMENT OF INDUSTRY
ASHDOWN HOUSE
123 VICTORIA STREET
LONDON SW1E 6RB
TELEPHONE DIRECT LINE 01-212 3301
SWITCHBOARD 01-212 7676

Secretary of State for Industry

25 February 1983

EXCHEQUER
REC. 25 FEB 1983
ACTION PS / C+E 25/2.
COPIES TO CST, FST, EST, MSTC, MSTR, Sir D Wass, Sir A Rawlinson, Mr Lovell, Mr Byatt, Mr Middleton, Mr Chivers, Mr Kemp, Mr Burns, Mr Burgess, Mr Gordon. Mr Moore, Mr Wicks PS/IR

The Rt Hon Sir Geoffrey Howe QC MP
Chancellor of the Exchequer
HM Treasury
Parliament Street
London SW1

For advice.
§8-Lon?

Dear Geoffrey,

1983 BUDGET

I have seen a copy of Nigel Lawson's letter of 8 February on this subject. I have written to you already on the subject of motoring taxes but I would like to add my comments now on the other topics raised in his letter.

2 I strongly endorse Nigel's proposal that there should be no increase in HFO duty or in the associated duties on gas oil, avtur and lubricating oils. I regret that this is the most we can do but appreciate that the idiosyncracies of the Frigg gas contract would make abolition of HFO an expensive option, in relation to the benefits which it would confer on industry. But equally, non-valorisation is also the very least we can offer industry to mollify their justifiable sense of grievance about HFO duty. I hope, therefore, that you will feel able to accept Nigel's proposal.

? Not Budget

3 The proposal to extend the Coal Firing Scheme to 31 March 1984 is one of several options currently being considered by officials and I hope to write to colleagues shortly on this subject. To anticipate these deliberations a little, I think that it will be difficult to resist the strong pressures we are under to provide some extension to the scheme - though not necessarily as long as one year - in view of the fact that Community loans in support of the scheme only became available in November 1982.

4 Nigel's other proposal for encouraging energy saving is a loan guarantee scheme. I would also like to see some additional support for energy efficiency but I am not sure that a loan guarantee scheme would be the most appropriate vehicle for providing this.

5 The Loan Guarantee Scheme which is currently in operation is directed towards small firms, many of whom would have difficulty attracting finance, because of their lack of track record. The firms in difficulty on energy costs are in a different position since they are typically large firms with a long track record. Their problem is that because of the recession, a high sterling exchange rate over the last three years, coupled with disadvantageous energy costs, their capacity for borrowing has been stretched, in some cases to the limit.

6 These firms would require grants at the same level as is provided under the Coal Firing Scheme, supplemented possibly by EIB loans in respect to the balance of project costs, if they are to be able to invest in energy conservation on a substantial scale.

7 It is, of course, open to these companies to apply for Selective Financial Assistance under Section 8 of the Industry Act. It may, however, be necessary to consider a separate energy efficiency scheme, firstly because the level of support normally offered under SFA - in the region of 10% of eligible costs - may be insufficient to stimulate investment in energy efficiency; and secondly, because the minimum threshold for eligible costs - £½ million - would rule out a number of energy conservation investments. There are, of course, problems in identifying the energy conserving elements in investment projects. I would be happy for my officials to discuss the details of such a scheme with Nigel's.

8 Finally, I would urge you to consider some small additional provision for help on electricity prices, in addition to the provisions already made for next year. You will know that last week Nigel and I met representatives of the major energy-consuming industries who made it abundantly clear that, even with the changes which Nigel has achieved and the benefits of the Sterling depreciation, there remain a number of major electricity consumers whose disadvantage in respect of electricity costs remain significant. I shall be writing to Nigel shortly with some further proposals for relief, but one straightforward way of assisting some of them would be to lower the threshold for eligibility to the CCL scheme from 6MW to 3MW. This reduction would make the CCL terms available to a number of small electricity-intensive users. According to the paper industry, for example, 26 of its producers would qualify for CCL terms rather than the 9 which qualify at present. A number of small steel producers would also benefit. I recognise that quite a number of large but not particularly intensive users would also qualify, raising the potential cost of halving the threshold but I doubt whether many of these would in practice be prepared to accept the constraints imposed by the CCL terms.

This change would have a modest cost, and would help to ease the problems of a number of companies worst hit by the recession.

9 I am copying this to Nigel Lawson and George Younger.

Yours ever

Patrick

pup

IDT BUDGET ARRANGEMENTS 1983

I attach IDT's revised draft Budget Day programme for 15 March.

J. Page

J PAGE
28 February 1983

Distribution

IDT
Mr Hall
Miss Collins
Mr Monaghan
Mr Macrae
Mr Towers
Mr Evans
Mrs McKinney
Miss Edwards
Mr MacKellar
Mr Segal
Mr Haydon
Mr Johnson
Mrs Gambling
Miss Wilding
Miss Vasili
Mrs Wilkins
Mrs Stirton

EB
Mr R I G Allen
Mr Collins

CU
Mr Norgrove
Mr Corcoran

COI
Mr J Barrows

PRIVATE OFFICES
Mr Kerr
Miss O'Mara
Miss Rutter
Miss Young
Mr Brazier
Mr Gieve
Miss Swift
Mr Donnally
Mr Kwiecinsky
Mr Harrison
Miss Pollock
Mr Bush
Mr Hudson

Mr Milner

Mr Williams
Mr Slaughter
Mr C Rowley

Mr Salveson

EOG
Mr Chambers
Mr Carpenter
Mr Uden
Mr Batchelor
Mr Bobsin
Mrs Mills
Mr C Ludlow
Mrs McGill
Mrs Bugden
Mr A Robertson

GEP
Mr Mountfield
Mr Hart

PE1
Mr J Richardson

Mr B Ingham, NO 10 (two copies)

Mr P Lewis, Inland Revenue
Mr J Dahn, Customs and Excise
Mr D Davey, NO. 11

✓

MAIN ALLOCATION OF IDT RESPONSIBILITIES

Private Office: House: Lobby Liaison	Mr Hall
Budget Broadcast	Mr Hall
Control of IDT's administrative preparations for and performance on Budget Day including:	Mr Monagham (JM) Mr Page (JP)
1) March 12 Chancellor's Photocall (assisted by Mrs McKinney)	JM
2) March 15 Chancellor's Photocall (assisted by Mrs McKinney)	JM
3) Ministerial Broadcasts on March 15 (prior collation of TV/Radio bids for Ministers excluding the Chancellor): Mr MacKellar)	JM
4) Monitoring of TV/Radio Budget transmissions; and advice to Mr Hall on TV/Radio reaction to Budget. (assisted by Mrs McKinney with preparations before March 15 ie. installation of equipment, organisation of monitoring teams; and assisted by Mr MacKellar on Budget Day.	: JM
5) Sectional release of Speech in external TV/Radio Studios and at Financial Times.	JP
6) Release of documents in the Gallery, to the Lobby and to the Press at HMT. R/29. (assisted by Mr Haydon, Miss Young and Miss Vasili in the Gallery, and by Mr Johnson, Mr Richardson in HMT 2/29.	JP

Re 5 Sectional speech release in external studios

Treasury representatives outside the office: (with full sectional texts of speech for simultaneous release in Studios and Newsrooms)

		1983 Team
1	BBC Television Studio	Mr Eric Kwiecinsky
2	BBC Radio Studio	Miss Jane Swift
3	ITN Studio	Mr Jim Milner
4	IRN Studio	Miss Theresa Pollock
5	Press Association Newsroom	Mr Duncan Slaughter
6	Financial Times Newsroom	Mr Colin Rowley

Final vetting of document distribution list	Mr Johnson Mr Richardson
Collation/Distribution of Documents in CRU	Mr Johnson Mr Richardson Mrs Wilkins Mrs Stirton (plus two CAs)
Supervision of callers at front door	Mr Johnson Mr Richardson Mrs Mills + Security Officers
Distribution of documents to press and others	Mr Johnson Mr Richardson Mrs Wilkins Mrs Stirton Miss Wilding
Arrangement of COI facilities (teleprinter, car park permit, passes, etc.)	Mr Johnson Mr Richardson Mr Uden
Duty Press Officer (Budget evening)	Miss Edwards
Press Office: Telephones	Mrs Gambling
Press Office: Typing	Miss Wilding

CONFIDENTIAL

BEFORE THE BUDGET

Saturday 12 March — Mr Monagham
Weekend photographs of the Chancellor — Mrs McKinney

BUDGET MORNING

1. Mr Johnson to supply Mr Bobsin with names of BBC crew preparing for Chancellor's Budget Broadcast from No 11. Mr Bobsin to supply a Security Guard throughout day at No. 11.

2. By 10.30 am bulk copies of all Press Notices for IDT use to be sent by Divisions and other Departments to Mr Batchelor, in CRU.

3. Mr Page and Mr Haydon to check arrangements at the House of Commons. Mr Johnson and Mr Richardson to contact Security Officials and messengers who will work with them later in the day to make certain that they know where and when they are needed.

4. Mr Johnson and Mr Richardson to liaise with Mr Batchelor on document production/collation and to visit CRU and Committee Section and check that all facilities are available.

5. Mr Johnson to confirm with Mr Batchelor that the planned numbers of documents including Command Papers are available.

6. Mrs McKinney to check television and radio sets and direct lines to Studios and PA inthe respective monitoring rooms.

7. [Mrs McKinney to liaise with Mr Monaghan and arrange informal photocall at No. 11 for evening papers. (If Chancellor is available).]

8. Mr Johnson and Mr Richardson to finalise document distribution lists.

9. Mr Uden to deliver 2 radio sets to Mr Johnson for use in IDT.

10. Mr Collins, EB, to ensure that headlines and sidelines are provided for the nine unstapled copies of the Speech which go to PA, Reuters and the main Broadcasting studios. He will bring two copies to Mr Hall for the House (Reuters and PA). Mr Brazier

will give six copies to Mrs Willis for the studio packages and one copy to Mrs Gambling for the Press Association Newsroom. Mr Slaughter will collect the PA copy from Mrs Gambling at 3 pm to take to the House of Commons Press Gallery.

11. At noon, Mr Hall to collect 18 copies of the Budget Speech, Snapshot, Financial Statement and Budget Report (FSBR), Command Papers, and all press notices from Mr Brazier in the Chancellor's Office.

12. Mr Evans to bring 18 copies of the Brief on return to IDT from EB.

13. Mr Johnson and Mrs Wilkins to collate documents in Mr Hall's room (93/2) and address complete sets in folders as follows:-

Mr Hall		(2 sets, in separate folders; one without EB Briefs to be given to Mr Samuel Brittan in the Press Gallery at the end of the Speech).
Mr Monaghan		
Mr Macrae		
Mr Page		
Mr Towers		
Mr Segal		
Mr Evans		
Miss Edwards		
Mr MacKellar		
Mrs McKinney		
Mr Johnson		
Mr Barrows	(COI)	(Three sets, in separate folders but no copy of Briefing).
Mr MacKellar		(Two sets for monitoring team to be returned to Mr Page at end of monitoring operation).

14. At 1.00 pm or soon after, Mr Hall to brief IDT and the COI writers, to hand them their personal Budget documents and to advise them of any material that might be expected later.

will give his copies to Mr Hollis for the usual purposes and any copies for checking for the [illegible] [illegible]. Mr [illegible] will collect the [illegible] from the [illegible] at 7 pm to take to the House of Commons Press Gallery.

11. As soon, Mr Hall to collect 15 copies of the Budget Speech Snapshot, Financial Statement and Budget Report (Red Book) [illegible] Papers, and all press notices from Mr [illegible] in the Chancellor's Office.

12. Mr [illegible] to bring 10 copies of the [illegible] [illegible] from [illegible].

13. Mr Johnson and Mrs Wilkins to collect documents in Mr Hall's room (15/1) and address complete sets in folders as follows:-

Mr Hall	10 sets, in separate folders, one [illegible]. [illegible] to be given to Mr [illegible] in the Press Gallery at the end of the Speech.
Mr Robertson	
Mr [illegible]	
Mr Page	
Mr [illegible]	
Mr Hughes	
Mr Evans	
Miss Edwards	
Mrs [illegible]	
Mrs [illegible]	
Mr Johnson	
Mr Harrison (1 copy)	[illegible], in separate folders, [illegible]
Mr [illegible]	[illegible]

14. [illegible]

15. Mr Hall to check that the "page-by-page" copies of the Speech, which he hands out to PA and Reuters in the Press Gallery, are marked with numbered red "ears" denoting the end of each section. Mr Johnson to arrange this with Mr Brazier.

16. Mr Norgrove to bring final text of Guidance telegram to Mr Monaghan in Room 92/2.

17. Following Mr Hall's briefing, the Press Officers and COI writers take their copies of the Budget papers and remain without telephone contact in Rooms 88, 89 and 90/2 until the end of the Speech.

18. The COI team, under Mr Barrows, will assemble in Room 107/2.

19. At 1.30 pm two clerical assistants to be nominated by Mr Robertson to report to Mrs Wilkins in Room 109/2.

20. At 1.30 pm Mr Towers will take up duty as "Anchor Man" in 92/2. At the same time Mrs Gambling will switch the three main Press Office telephone lines to the answering machine. The message on the tape should say:-

> "The Press Office is closed until the end of the Chancellor's Speech in the House of Commons. If your enquiry is urgent, please call Mr Towers on 233-3464

21. Normal telephone service will be restored immediately the Chancellor sits down.

22. At 2.30 pm, Mr Haydon meets four messengers in R75A/G to collect documents for the Lobby. They will take these to the Chancellor's room at the House of Commons where they will leave them in the care of a Security Officer until they are collected by Mr Haydon Miss Young and Miss Vasili at the end of the Chancellor's speech.

23. At about 2.45 pm, Mr MacKellar to go to Number 11 to control photographers at Chancellor's departure and to supervise the Financial Times photographer and the TV camera crews.

15. Mr Hall to check that the Press Gallery copies of the Budget, which he [illegible] out to PS and [illegible] in the Press Gallery, are [illegible] with envelopes and "Secret" [illegible] the end of [illegible]. Mr [illegible] to arrange this with Mr [illegible].

16. Mr [illegible] to bring [illegible] of [illegible] to Mr [illegible] in Room [illegible]

17. Following Mr Hall's reporting, the Press Officers and [illegible] take their copies of the Budget papers and remain in telephone contact in Rooms [illegible] until the end of the Speech.

18. The COI team, under Mr [illegible], will assemble in Room [illegible].

19. At 1.30 pm two clerical assistants to be nominated by Mr Robertson to report to Mrs Wilkins in Room [illegible].

20. At 1.30 pm Mr [illegible] will take up duty as "Anchor Man" in [illegible]. At the same time Mrs [illegible] will switch the Press Office telephone lines to the answering machine. The message on the tape should say:-

"The Press Office is closed until the end of the Chancellor's Speech in the House of Commons. If your enquiry is urgent, please call [illegible]."

21. Normal telephone service will be restored immediately the Chancellor sits down.

22. At [illegible] pm [illegible] four messengers [illegible] for the [illegible]. They will then [illegible] of the House of Commons where they will [illegible] at a Security [illegible] until they are [illegible] Miss [illegible] and Miss [illegible] at the end of the Chancellor's [illegible].

23. At about 2.45 pm Mr [illegible] to go to Number 11 to [illegible] the Chancellor's [illegible] and to [illegible] the Financial Times photographer and the TV camera crews.

24. The Chancellor to be reminded to time his departure from Number 11 to meet the TV timings agreed earlier in the day.

25. At 3 pm, Mr Monaghan takes the prepared documents for the Monitoring teams to Rooms 110/2 and 112/2 to meet the media representatives and to introduce the monitoring officials.

26. [At 3.05 pm Mr Haydon to be in the Chancellor's room at the House of Commons to meet FT photographer and to remain with him for the brief photo-session when the Chancellor arrives]

27. When photo-session is over, Mr Haydon will move next door to the Chancellor's waiting room to join Miss Young and Miss Vasili. Assisted by Security Staff, they will take 30 copies of the speech in sections, 50 copies of the complete speech and 60 copies of the "Snapshot" in a separate package, to the Press Gallery. They will also have a separate package of 10 copies of the Speech and 10 copies of the Snapshot for the Overseas Press.

28. Mr Haydon will remain behind the barrier in the Gallery throughout the Speech and release the sections of the Speech to the Secretary of the Gallery, Mr William Russell, on instructions from Mr Hall (signalled by the pages with red "ears"). At the conclusion of the Speech he will release the final packages of the complete speech before leaving for the Lobby Room, to distribute documents there.

29. HF/3 to insert Budget highlights on Reuters VDU, as previously agreed between by Mr R Evans and Mr Turnbull and Miss Greenwood.

30. Mr MacKellar will ask monitors to take notes of significant comment by media presenters or commentators so that he may prepare a short brief for Mr Hall to present to the Chancellor before he sees the Lobby. Mr MacKellar to provide advice by phone, based on monitors' assessments, to Mr Hall in the House.
Officials in the monitoring team are reminded that they can give guidance only on those sections of the Speech which have been completed.

24. [and Chancellor to be escorted to room [illegible] [illegible] Room/11 to meet the TV [illegible]

25. At 3 pm, Mr [illegible] takes the [illegible] statement for the participating teams in Rooms [illegible] and [illegible] to meet the media [illegible] and to introduce the [illegible] officials.

26. [At 3.30 pm Mr Haydon to be in the Chancellor's Room at the House of Commons to meet TV photographer and to remain with him for the brief photo-session when the Chancellor arrives]

27. When the question is over, Mr Haydon will move next door to the Chancellor's waiting room to join Miss [illegible] and Miss [illegible], escorted by Security staff. They will have [illegible] copies of the speech in envelopes, [illegible] copies of the [illegible] and [illegible] copies of the "Statement" in a separate package, to the Press Gallery. They will also have a separate package of 10 copies of the Speech and 10 copies of the [illegible] for the Overseas Press.

28. Mr Haydon will remain behind the Speaker in the Gallery throughout the Speech and [illegible] the [illegible] of the speech to the reporters of the Gallery, by [illegible] [illegible] from Mr Hall [illegible]. At the conclusion of the Speech he will release the "final sections" of the [illegible] for the [illegible] [illegible].

29. [illegible]

30. Mr [illegible] will [illegible]

31. Mr Barrows and his assistants (COI) will assemble in 107/2 with three sets of documents and a radio set. Mr Barrows will remain in Room 107/2 until the Speech is finished. As the Speech progresses, he will mark up the completed sections and have them sent to the COI as follows:-

a) One section of the edited version of the speech to the COI telex operator.

b) One section of the Speech to the COI driver in the Centre Courtyard.

32. At about 2 pm Mrs Wilkins and her assistants will go to Committee Section (Room 75/G) to supervise the packaging of copies of documents according to the prepared lists.

33. Mrs Wilkins will immediately package one copy of the Speech to hand to Mr Colin Rowley for the Financial Times. Mr Rowley will then go straight to the courtyard where a car will be waiting to take him to Bracken House.

34. At 4.30 pm, two messengers report to Mrs Wilkins in Room 75/G to await instructions to take prepared envelopes to Room 29/2 in readiness for distribution at end of Speech. Mr Uden will provide four trolleys for this operation.

AT END OF SPEECH

a) House of Commons

35. At end of the Chancellor's speech, after releasing the final packets of documents to the Secretary of the Press Gallery, Mr Haydon and Miss Vasili take the packaged papers from the Chancellor's room to the Lobby Room (without waiting for Mr Hall) and distribute them to correspondents in advance of the Chancellor's arrival.

36. Mr Hall will hand over the standard package of documents to Mr Samuel Brittan before leaving the Press Gallery at the end of the Speech to join the Chancellor in his room at the House. He will await a telehone call from Mr MacKellar informing him

of Radio and TV reaction to the Speech.

37. Later, Mr Hall will rejoin the Chancellor after he has spoken to the Conservative Finance Group and escort him to the Lobby meeting.

b) Distribution of Documents at Treasury

38. Callers have been invited for "about 4.30 pm". Security staff will register names of callers and provide escorts.

39. Non-Press callers will be asked to present their order forms.

40. Press and non-Press callers will be escorted to 29/2 to await release of documents. They should be seated in the areas clearly market "Press" and "Non-Press".

41. Official callers (Whitehall departments, embassies etc.) will be directed to the Enquiry Room.

42. When Mr Johnson gets the "release signal" from Private Office, he and Mrs Wilkins will take the prepared Press and non-Press envelopes to Room 29/2 where they will supervise distribution.

43. Envelopes for "official" and departmental callers will have been delivered earlier by Mr Johnson to Mrs Mills for distribution from the Enquiry Room.

44. Any "difficult" callers who have not ordered copies should be referred to Mr Richardson.

c) Press Office

45. Telephone service will be restored in IDT Press Office which will be manned by: GMc R, NT, RE, L.McK, EE.

46. At 5 pm, (FCO) will collect their copy of the Guidance Telegram from Mr Monaghan.

47. [COI Radio to join Mr MacKellar at No 11 for the Chancellor's "London Line" recording].

LATER

48. Mr Hall will return to No. 11 with the Chancellor after the Lobby meeting for last minute alterations, if any, to the Budget broadcast text.

THE NEXT MORNING

49. Mrs Maddock will arrive as early as she is able to start work on preparing transcripts of the previous evening's Ministerial broadcasts. Press Officers who have noticed points of special interest should guide her in her selection.

50. All Treasury Press notices issued on Budget day to be sent to those on the mailing lists.

51. Three part Press Summary to be prepared, as listed below:

Mr Towers	:	Budget Leader Comment
Mrs McKinney	:	Budget Feature Comment
Mr Evans	:	Non Budget items

Confidential

Mr Ken Brazier

Treasury Chambers
Parliament Street London SW1P 3AG

Telex 262405

Telephone Direct Line 01-233 } 7597
GTN 233 }
Switchboard 01-233 3000

William Russell Esq
Hon Secretary
Press Gallery
House of Commons

Your reference

Our reference

Date
28 February 1983

Dear Mr Russell,

BUDGET DOCUMENTS: MARCH 15 1983

I confirm that we propose to provide the following Budget Documents to the Press Gallery on Budget Day.

a. Martin Hall, the Chancellor's Press Secretary, will be in the Gallery throughout the speech and will release 2 copies of the text on a page-by-page basis to the Press Association and Reuters.

b. A Treasury official outside the Gallery will release 30 copies of the Chancellor's speech in SECTIONS to Mrs Stella Thomas as each section is concluded.

c. At the end of the speech this official will release 50 copies of the complete speech text together with 60 copies of the Budget Snapshot.

In addition he will hand to Mrs Thomas a separate envelope with 10 copies of the text and 10 copies of the Snapshot to enable you to cope with any requirements from Overseas Correspondents.

As soon as the Gallery distribution has been completed the Treasury official will go directly to the Lobby room, in advance of the Chancellor's arrival, and distribute the following documents.

45 copies of the Budget speech
60 Copies of the Financial Statement and Budget Report (Red Book)
60 Copies of the Budget Snapshot
60 Copies of Budget Press Notices

As you can see these arrangements follow those of previous years. I would be grateful if you could let me know if they meet with your approval.

I am copying this letter to Mr Warden as confirmation of our arrangements for the Lobby,

Yours Very Truly
John Page

JOHN PAGE

Confidential

C,

FROM: MISS J M SWIFT
DATE: 28 February 1983

PRINCIPAL PRIVATE SECRETARY

cc Financial Secretary
Economic Secretary
Minister of State (C)
Minister of State (R)
Sir D Wass
Sir A Rawlinson
Mr Byatt
Mr Middleton
Mr Kemp
Mr Burns
Mr Burgner
Mr Moore
Mr Wicks
PS/IR
PS/C&E

1983 BUDGET

The Chief Secretary has seen Mr Jenkin's letter of 25 February.

2. The Chief Secretary thinks it extraordinary that Mr Jenkin should put forward the proposal (paragraph 8) to lower the threshold for eligibility to the CCL scheme from 6MW to 3MW without any estimate of the cost. The Chief Secretary really does not think we should go along with this proposal in any way.

C/
You asked about the cost of the ¶8 proposal. Nigel Wicks' best guess is £30m but it could be considerably less. In the normal course, we'd approach D/Energy to find out or we'd prompt them to write in (they didn't even think the idea worth backing themselves). But CST is very opposed to any stirring up. Unless you want them to pursue it, PE will therefore put up only qualitative advice.

MOM
28/2

MJS

MISS J M SWIFT

FROM: CHIEF SECRETARY
DATE: 1 March 1983

cc Sir D. Wass
Sir A. Rawlinson
Mr Bailey
Mr Mountfield
Mr Kemp
Mr Monger
Mr Pestell

CHANCELLOR

You wanted to look again at the 'envelope' note below. JW

See S.A.G. mar 1. §4 ii

BUDGET PUBLIC EXPENDITURE - FINANCING CHILD BENEFIT

Following our discussion with Norman Fowler last night and our subsequent chat, I have been giving some further thought to the overall public expenditure component of the Budget packages and to the increase in child benefit.

2. As you know, I am now convinced that we should raise child benefit to £6.50 a week. However, that involves an extra cost of £20 million in 1983-84 and £50 million in the full year compared with the package we agreed with Norman Fowler last night. I am, in any case, slightly concerned that the total public expenditure increase involved in the present draft packages may be uncomfortably high given the latest assessment of likely bids on the Contingency Reserve next year.

3. I propose, therefore, that we should make some reductions in the public expenditure components of the construction and innovation packages, namely:

- drop the extension of the home improvements scheme to inter-war houses, saving £25 million, and
- deduct £5 million each year from the innovation package involving £3 million reductions from the proposed increase in advisory services and £2 million from computer aids and software.

4. This would more than offset the additional cost in 1983-84 although it would leave a substantial net additional cost in 1984-85 in later years. I attach a note by Mr Godber which sets out

a convincing case, in my view, for giving priority to enveloping within the construction package. The selection of items within the innovation package also reflects views of officials here. The reductions would still leave substantial and attractive packages.

5. I think it most important that we should make it plain to Norman Fowler that we are still holding him to a "nil net cost" package and that the 10p increase in child benefit over and above that has been offset by reductions in other elements of the Budget.

6. Finally, I have not looked for further reductions in the £25 million provisionally set aside for employment measures. We are to discuss the proposals tomorrow but the position on child benefit and the forecast underline once again how important it is for us to resist a nationwide extension of enterprise allowances.

L.B.

LEON BRITTAN

Confidential

FROM: S A GODBER
DATE: 1 March 1983

SIR ANTHONY RAWLINSON

cc Mr Mountfield
Mr Pestell

ENVELOPING

As agreed, I have checked with DOE how an enveloping initiative might be run.

2. Ideally, they would like an unlimited scheme ie one in which all approved schemes carry with them an additional capital allocation. They agree with my estimate that this would, at most, result in £50m of additional allocations. But there would be no need to announce a figure - just that all schemes would be assisted.

3. If a limit has to be put on the expenditure - at whatever level - then DOE would favour a 'first come first served' approach. But they fear that many authorities would be put off even trying in case the planning work was wasted.

4. Like me, and (I think) the Chief Secretary, DOE officials would give a higher priority to enveloping then to improvement grants; and within i mprovement grants they would favour action on eligible expense limits not inter-war houses. The main points are:

(i) local authorities are heavily overloaded with applications for improvement grants already

We need to say this

(ii) the initiative in the last Budget is due to run out at the end of 1983-84; and extension of the scheme now would add to pressure to continue the higher grant rates beyond 1983-84.

(iii) if the improvement grant system is to be substantially revamped after the election (as all agree it should be), now is not the time to be extending it in ways which may not be consistent with long term aims.

(iv) enveloping is not only potentially more cost effective than improvement grants, it is also new - further action on improvement grants is not.

(v) expenditure on repairs grants has proved very volatile following the last Budget. We cannot predict at all accurately what the impact of allowing repairs grants for interwar houses would be.

5. We do not know what DOE Ministers' views would be but it seems likely that they would not mind missing out on repairs grants for interwar houses if that would allow them to run an unlimited enveloping scheme instead of one limited to, say, £25m. They would also probably give a higher priority (as I would) to increasing eligible expense limits (currently £5000 in London and £4000 elsewhere) than to inter-war houses.

6. You asked about typical enveloping schemes. The range is probably 50-200 houses. The smaller schemes could be completed in 1983-8 4, the larger would take longer. Average cost will be £7-8000 per house. This gives an average 1983-84 cost of £0.5 - 1m per scheme. Thus, in an unlimited system we might expect 70-80 schemes to be undertaken ie 15-20% of local authorities might take up the offer. If only £25m were available, perhaps 40 schemes could be supported.

7. Two minor points:

(i) the first enveloping scheme to be financed through the housing programme is due (if we approve it) to start on site in Newport on 16 March.

(ii) DOE put the stress on the first syllable of enveloping.

S A GODBER

NOTE A

1 March 1983

BUDGET MEASURES

£ million PSBR costs indexed

	1983-84		1984-85	
Prior Claims				
✓NIS - ½% from August	200		300	
✓IT - 8½ over RW - bare basic*	990		1040	
CB - lower rate contemplated**	[60]		[175]	
Total Prior Claims		1190		1340
Group A				
✓Specific Duties - net***	(10)		(10)	
Oil - Package B plus Condoc concessions	95 110		85	
✓CT - Package 6(b)	35		60	
IT - roundings on allowance*	20		20	
CB - higher rate contemplated**	[20]		50	
Unemployment Measures How much more housing?	[25]		25	
Package elements (see attached Note C)	125	265	205	435
Total Prior Claims + Group A		1455		1775
Group B				
MIRC - upper end of costs of going to £30,000	70		85	
ACT - extension of carry-back 6 years	-		60	
DTR - reverse ACT/DTR set off	-		~~35~~	
Package elements - other (see attached Note C)	65	135	65	245
Total Prior Claims + Group A + Group B		1590		2020
Not reflected				
Social Security (?) (Revenue cost)****	0-30		0-90	

* This is the basic cost of 8½ per cent over RW. In Group A is the additional cost of rounding the married man's allowance. Other permutations are possible.

** CB and unemployment measures are public expenditure. Of the total cost £100 about million and £175 million (1983-84 and 1984-85) are scored at nil for the Budget arithmetic being covered by public expenditure shortfall already allowed for in the forecast. All the other public expenditure elements in the Budget are charged at full PSBR cost.

*** Gains on cider and VED, less costs on tobacco, petrol and derv concessions.

**** Net cost after offsetting unemployment benefit and caring proposals.

BUDGET SECRET

Note B

1 March 1983

FOR DETAILS OF MEASURES SEE NOTE A

£ million revenue costs indexed

	Persons 1983-84		Businesses 1983-84		Persons 1983-84		Businesses 1983-84	
Prior Claims								
NIS*			570				800	
IT	1150				1450			
CB	60				175			
Total Prior Claims		1210		570		1625		800
Group A								
Specifics			(10)				(10)	
Oil			105				100	
CT			40				70	
IT	20				40			
CB	20				50			
Unemployment			25				25	
Packages	5	45	133	293	(10)	80	250	435
Total Prior Claims + Group A		1255		863		1705		1235
Group B								
MIRC	75				100			
ACT							70	
DTR							40	
Packages	27	102	48	48	5	105	76	186
Total Including Prior Claims, Group A, Group B and Autumn ½% NIS. Tax and P/Ex.		1357		911		1810		1421
Total revenue costs - Budget only indexed**			1620				2215	
Total revenue costs - Budget only unindexed**			1900				2750	

* ½% August '83 plus ½% Autumn '82

** As in FSBR (provisional figures). Excludes P/Ex elements charged to reserve or otherwise absorbed in existing totals.

NOTE C

1 March 1983

PACKAGES

£ million revenue costs

	1983-84				1984-85			
	Group A		Group B		Group A		Group B	
Enterprise and Small Firms (Table A)	(B)	28			(B)	146		
except CTT*			(B)	23			(B)	46
Technology and Innovation (Table B)	(B)	44			(B)	84		
Construction (Table C)	(B)	60			(B)	20		
except some cutting down on enveloping and/or improvement grants			(B)	25				
Caring and Charities (Table D)**	(P)	5			(P)	27		
except Widows Bereavement			(P)	25			(P)	30
Miscellaneous and "Fairness" (Table E)	(B)	1			(P)	(37)		
except "publicans mortgages"			(P)	2			(B)	5
Total revenue costs as Note B		138		75		240		81
Reduce to PSBR costs (say)		13		10		35		16
Total PSBR costs as Note A (say)		125		65		205		65

Revenue costs split (say)

	1983-84 Group A	1983-84 Group B	1984-85 Group A	1984-85 Group B
Businesses (B)	133	48	250	76
Persons (P)	5	27	(10)	5

* CTT taken as "businesses" in this analysis as part of enterprise etc package. But it could be described as "persons". (There are other items which can score both ways or not at all).

** "Caring" package costs (and unemployment benefit proposals) scored net

TABLE A

DATE: 1 March 1983

BUDGET PACKAGES [Note: items marked * are public expenditure]

SMALL FIRMS, ENTERPRISE AND WIDER SHARE OWNERSHIP

		1983-84	1984-85	Full Year
1.	Business Expansion Scheme	nil	75	75
2.	Loan Guarantee Scheme*	nil	nil	-
3.	Wider share ownership	20	30	35
4.	Capital Gains Tax (see note)			
	(a) monetary limits	nil	1	1
	(b) retirement relief	nil	1	4
5.	VAT registration thresholds	5	10	10
6.	De minimis limit for assessment of apportioned income	under 1	under 1	under 1
7.	Acceptance credits	1-2	1-2	1-2
8.	Capital Transfer Tax (see note)	23	46	55
9.	Zero/deep-discounted stock (under discussion)	neg	25 15/20 ?	75
10.	Relief for interest, employee buy-outs	1	1	2
11.	Close companies - ACT limit on loans (depends on mortgage interest relief ceiling but assumed dead)	-	-	-
12.	Tax treatment of interest paid by companies to non-residents (Revenue submission to come)	under 1	under 1	10
	GRAND TOTAL	51	192	268

Notes: (1) For item 4 of the cost of the measures when statutory indexation is taken into account is nil, 5 and 15 million.
(2) For item 8 the cost of the measures when statutory indexation is taken into account is 38, 76 and 90 million respectively.

TABLE B

DATE: 1 March 1983

BUDGET PACKAGES

TECHNOLOGY AND INNOVATION [Note: items marked * are public expenditure]

		1983-84	1984-85	1985-86
1.	Extension of transitional period for capital allowances - films	nil	nil	30
2.	Extension of transitional period for capital allowances - teletext TVs	nil	10	15
3.	SEFIS*	20	40	40
4.	Information technology*	7	10	13
5.	Innovation linked investment*	5	15	20
6.	Advisory services*	12	9	9
7.	Science Parks* (see note)	-	-	-
	Revenue costs	nil	10	45
	Public expenditure costs	44	74	82
	TOTAL PACKAGE COST	44	84	127

Note: The total public expenditure cost over three years is £200 million; the science park cost is to be accommodated within this total. The cost of the whole package over three years is £255 million.

DATE: 28 February 1983

BUDGET CONFIDENTIAL

TABLE C

DATE: 1 March 1983

BUDGET PACKAGES [Note: items marked * are public expenditure]

CONSTRUCTION

		1983-84	1984-85	Full Year
? 1.	Enveloping*	50	nil	-
? 2.	Improvement grants*	35	nil	-
✓ 3.	Increase in proportion of office space qualifying for industrial building allowance	nil	10	25
4.	Increase in hotel allowance or extension to self catering (CST minute to Chancellor 24.2.83).	nil	up to 5	up to 5
✓ 5.	DLT - extension of own-use deferment	nil	under 1	4
✓ 6.	Small Workshop Scheme - averaging for converted premises	under 1	under 1	under 1
	Revenue costs	nil	15	40
	Public expenditure costs	85	nil	-
✓ 7.	Stock relief: householders part exchange - simple scheme.	under 1	5	5
X 8.	Extension of assured tenancy capital allowance to shared ownership properties (still under discussion with DOE)	na	na	na
	GRAND TOTAL	85	20	45

BUDGET CONFIDENTIAL

TABLE D

DATE: 1 March 1983

BUDGET PACKAGES

CARING AND CHARITIES [Note: items marked * are public expenditure]

		1983-84	1984-85	Full year
ALL ITEMS STILL OUTSTANDING				
1.	Extension of widows bereavement allowance	25	30	30
2.	Real increase in mobility allowance*	2	6	-
3.	Real increase in therapeutic earnings limit*	0.1	0.3	-
4.	Abolition of £250,000 limit for CTT exemption - gifts to charities	under 1	under 1	under 1
5.	Deeds of covenant; increase in ceiling for higher rate relief to £5,000	nil	3	3
6.	New war pensioners mobility supplement*	0.2	2	-
7.	Supplementary benefit capital disregards*	3.5	11	-
8.	Tax relief for staff seconded by companies to voluntary bodies + ENT. AGENCY	under 1	under 1	under 1
9.	Removal of invalidity trap*	7.5	23	-
	Revenue costs	25	33	33
	Public expenditure costs	13	42	-
	Public expenditure costs after offsetting savings	nil	12	-
	TOTAL PACKAGE COSTS	25	45	33
10.	Real increase in housing benefit children's needs allowance*	3	10	-
11.	Grants to bodies involved in voluntary service for elderly*	2	2	-
	GRAND TOTAL	30	57	33

Note: All the public expenditure items in the package are subject to further discussions with Mr Fowler.

DATE: 28 February 1983

TABLE E

DATE: 1 March 1983

BUDGET PACKAGES

£m (yields) unless otherwise stated

MISCELLANEOUS (INCLUDING "FAIRNESS")

		1983-84	1984-85	Full year
? 1.	Fringe benefits - scholarships	neg	(5)	(5)
2.	Fringe benefits - car and car fuel scales - 14% or 15%	nil	(30)	(30)
3.	Fringe benefits - "Marks & Spencer" device	nil	nil	1
4.	Life assurance: chargeable events: secondhand bonds	under (1)	under (1)	under (1)
5.	CGT: non-resident trusts	under (1)	under (1)	under (1)
6.	CTT - remove special deemed domicile rule for offshore islands Cost:	1	2	2
7.	Group relief: avoidance (BL)	nil	(10)	(10)
? 8.	DLT: disposals by non-residents (MST (R) considering)	(1)	(2)	(2)
9.	Taxation of international business (consider with ACT/DTR change)	under (1)	under (1)	(100)
? 10.	Fringe benefits; double £25,000 device (depends on mortgage interest relief ceiling)	nil	under (1)	under (1)
11.	Directors PAYE tax	nil	(10)	(10)
12.	TSBs to be treated as bodies corporate	2	20 to be shaded down	20
13.	Stamp duty - selective reform package (awaiting Chancellor's final decision ? nil	-	-	-
14.	VAT exemption for work of art accepted in lieu of tax (Customs submission 23.2.83	1	1	1
15.	Self employed second home mortgage interest relief ("Publicans")	2	5	5
	GRAND TOTAL costs/yields	3	(32)	(132)

FROM: G S JOHNSON
1 March 1983

1. MR PAGE

2. MR BATCHELOR

CC: Miss O'Mara
Mr Brazier
Mr Chambers
Mr Hall
Mr Monaghan
Mr Haydon
Mrs Wilkins

BUDGET DOCUMENTATION

At our meeting last Friday, final figures were agreed for IDT Budget document requirements. I attach a schedule (Annex A) laying out IDT's consolidated needs. I consider that our requirements of the Snapshot will be larger than you can provide. In the event of the Enquiry Room exhausting their supply I trust CRU will be able to oblige us with some more copies on March 16.

To complete IDT's submission, I also attach a breakdown of the, in studio, documents (Annex B). This covers the sectioned and stapled/unstapled copies of the speech which will be taken to broadcasting studios and the House of Commons. There requirements are supplied by you to Mr Brazier from whom they are collected by individual members of the studio team. Details are set out in final version of Miss O'Mara's Budget Aide Memoire of recent date, paras

46 a) Press Gallery
" b) ITN Wells St
" c) BBC TV White City
" d) BBC Radio Broadcasting House
" e) IRN Gough Square
" f) Channel 4 (to be taken by Mr Milner to ITN)

Our counting of these documents is set out in Annex B.

G S Johnson

G S JOHNSON

BUDGET 1983

IDT'S CONSOLIDATED REQUIREMENTS (As agreed 25.2.83)

	Speech	Snapshot	FSBR	Other CMND Papers	HMT PNs	OGD PNs
Press Gallery	50	60	-	-	-	-
Overseas Reps	10	10	-	-	-	-
Lobby	45	60	60	60	60	60
Fleet St. Press	130	130	120	120	120	120
Non-Press	130	130	120	120	130	130
Dept's Press Officers	30	30	30	30	30	30
HMT Mail List	-	-	-	-	220	-
Spares, inc enquiry room	25	95	20	10	150	-
FFJG	-	20	20	-	-	-
TOTALS	420	535	370	340	710	340

ANNEX B (IDT Requirements supplied by Chancellor's Office)

1. Sectioned copies of the Budget Speech

Press Gallery	30	(para 46 (a))
BBC TV	10	
ITN TV	15	
BBC Radio	10	
IRN	4	

2. Nine Unstapled Copies of Speech: one each for PA and Reuters in House (with Red Ears); PA Newsroom; ITN; BBC TV; BBC Radio; IRN; Reuters (at 85 Fleet St)+ Financial Times

[+Added in place of Channel 4 copy, currently allocated].

3. Envelopes for Study and Newsroom Release

Each pack to contain:
- 1 stapled copy of speech
- 1 snapshot
- 1 FSBR
- 1 of Command Papers and Press Notices

PACKS

BBC TV	-	2
ITN	-	3 (incl. Channel 4)
BBC Radio	-	2
IRN	-	1
		8

[These figures do not coincide at all points with those in the latest Private Office Aide Memoire].

FH

CONFIDENTIAL

FROM: F MARTIN
DATE: 1 MARCH 1983

1. MR MOORE 7/1/3/3.
2. CHIEF SECRETARY

cc Chancellor
Financial Secretary
Economic Secretary
Minister of State (R)
Minister of State (C)
Sir Douglas Wass
Mr Middleton
Mr Kemp
Mr Robson
Mr Griffiths
Mr Salveson

PS/Inland Revenue

Mr P Lewis IR

PS/Customs & Excise
Mr Howard C & E
Mr P Graham,
Parliamentary Counsel

FINANCE BILL: AMENDMENT OF THE LAW RESOLUTION

We need in the near future to give Parliamentary Counsel instructions on the form of the Amendment of the Law Resolution for the Bill and on whether we are to have the usual Incidental Charges Resolution.

Amendment of the Law Resolution

2. As you will recall, every provision in the Finance Bill for a new tax, for increasing an existing tax, or for renewing an annual tax must be covered by a corresponding resolution of the House; and the Bill may not increase a tax above the level approved in the resolution.

3. Provisions for reducing taxation, for dealing with the machinery of tax administration, and for amending the law dealing with the National Debt are held to be covered by a general resolution, the Amendment of the Law Resolution (ALR). Without an ALR, it would be out of order for any Member to move new clauses or amendments which were not covered by a specific Resolution. The effect of omitting the ALR would therefore be to restrict the discussion of the Bill considerably, a step which has only been taken in unusual circumstances (for example, in 1974 before the General Election).

4. On the other hand, an ALR which left unlimited scope for debate would open the way to amendments - for example, on VAT and NIS - which are likely to have unacceptable consequences in either

revenue or administrative terms. Such amendments would have to be opposed by the Government, a process which would clearly be both conspicuous and contentious.

5. The standard ALR used in recent years (copy attached) has therefore been drafted so as:-

(i) to allow amendments reducing the rate of VAT across the board, but to exclude amendments intended to zero-rate or exempt any new items or to provide refunds of the tax;

(ii) to allow amendments reducing or abolishing the National Insurance Surcharge, but to exclude amendments introducing selective reliefs; but

(iii) not to exclude discussion of any other specific tax.

6. Neither Customs, the Inland Revenue, nor ourselves know of any reason why the ALR should be drafted so as to restrict the debate on any items in the Finance Bill other than NIS and VAT.

7. As regards NIS our view is that the standard form should be used, in order to close off amendments to provide selective relief to, for example, the West Midlands.

8. On VAT the potential problem this year, as last, is the VAT Reform Group, given that use of the standard ALR would preclude amendments or debate on relief for charities. You will recall that last year the Chief Whip was consulted on this question and came down in favour of the standard form. Our and Customs' view is that this should be used again this year. Of the three VAT items which are currently starters for the Bill, two (number 6 - preconsolidation amendments - and number 13 - power to include conditions on intending traders in regulations) will not open the way to amendments on VAT relief to charities, while Customs' legal advice is that the third (number 28 - relief for contracted out services) could open the way only to amendments so convoluted that they

You have now proposed that 13 sd. be dropped. GW.

would be unlikely to be selected. Hence the standard ALR will not be outflanked. And without it the Bill would, of course, be open not only to amendments on relief for charities but on other areas (sanitary protection etc) as well.

The Incidental Charges Resolution

9. Since 1959 the resolutions have generally also included an Incidental Charges Resolution: a copy of last year's resolution is also attached. This enables Members to move amendments and new clauses which are designed to relieve tax but which, because of some side effect, might in theory at least result in a tax charge and would otherwise be out of order. (An example would be a proposal to relieve tax by an improvement in industrial buildings allowances, the result of which might be an increased balancing charge on disposal.) It would be unusual to exclude such a resolution, and we recommend that one should be tabled this year in the standard form.

10. It would be helpful to have your decisions on the latter and on the form of the Amendment of the Law Resolution as soon as possible, in order to assist Parliamentary Counsel.

F Martin

F MARTIN

1. Amendment of the law

That it is expedient to amend the law with respect to the National Debt and the public revenue and to make further provision in connection with finance; but this Resolution does not extend to the making of—

(*a*) any amendment with respect to value added tax so as to provide—

(i) for zero-rating or exempting any supply;

(ii) for refunding any amount of tax;

(iii) for varying the rate of that tax otherwise than in relation to all supplies and importations; or

(iv) for any relief other than relief applying to goods of whatever description or services of whatever description; or

(*b*) any amendment relating to the surcharge imposed by the National Insurance Surcharge Act 1976 and applying to some only of the persons by or in respect of whom the surcharge is payable.

52. Relief from tax (incidental and consequential charges)

That it is expedient to authorise any incidental or consequential charges to any duty or tax (including charges having retrospective effect) which may arise from provisions designed in general to afford relief from tax.

NOTE OF A MEETING ON TUESDAY 1 MARCH 1983 AT 11.00AM IN THE CHANCELLOR'S ROOM, HM TREASURY

Present:-

The Chancellor of the Exchequer (in the Chair)
Chief Secretary
Financial Secretary
Economic Secretary
Sir Douglas Wass
Mr Middleton
Mr Robson
Mr Turnbull
Mr Willetts
Miss Rutter
Mr Ridley

Mr Crawley - IR
Mr Beighton - IR
Mr Stewart - IR

Mr Plenderleith - Bank

TAX TREATMENT OF DEEP DISCOUNTED STOCK

The meeting had before it the Financial Secretary's submission to the Chancellor (24 February 1983) setting out his recommendation on the tax treatment of deep discounted stock in the light of responses to the consultative document issued in January. Mr Monck's submission to the Chancellor of 11 January on the tax treatment of gilts, and the Financial Secretary's comment in his minute of 13 January were also relevant.

2. At the Chancellor's invitation the Financial Secretary explained the four options set out in his minute. Options (a) and (b) covering conventional and indexed stock respectively were already possible and required no further legislation. Option (c) involving a symmetrical income treatment on an accruals basis for deep discounted stock would be an innovation which he commended to the Chancellor for inclusion in this year's Finance Bill. The symmetrical capital treatment of deep discounted stock (which could be regarded as option (d) in his minute) was a proposal for which he had some

sympathy and on which he would welcome further discussion. He added that it seemed regrettably that many outsiders did not properly understand the tax treatment of unconventional corporate bonds: it was for example not yet fully understood that symmetrical capital and income treatments of indexed stock were already available. He hoped that the Budget and the Finance Bill would provide an opportunity to improve understanding on this. Mr Middleton remarked that some of the responses to the consultative document amounted to requests for an interest rate subsidy through the tax system conceding asymmetry. They would have to recognise that this was not on but as the Financial Secretary's minute pointed out, it would be possible to move some way from the current tax rules without conceding this.

3. The Chancellor asked whether option (c) would involve an overall reduction in total tax liability or whether it would merely be shifted through time. Mr Crawley said that the accruals treatment would involve "asymmetry" through time in that the borrower would get his relief against income annually for the discount as it accrued whereas the investor would not be taxed on his accrued income until sale or redemption. Over time the Revenue would get the same total of tax receipts though they would be worth less. The Revenue had no overriding objections to option (c). Sir Dougls Wass added that one of the attractions of option (c) to lenders would be the delay in discharging the tax liability on the accrued income though of course this advantage would diminish as inflation came down.

4. The Financial Secretary said that his fear was that not enough would happen as a result simply of implementing option (c) though many of the responses to the consultative document had asked for this option. He thought there was a case therefore for considering option (d). This would involve a symmetrical capital treatment of deep discounted stock. It would not raise problems of arbitrage. Given that symmetrical capital and income treatments were both

available on indexed stock already there was a clear logic in extending symmetrical income and capital treatments to deep discounted stock. He accepted however that one argument against this was that confusion would be caused by the wide variety of options available. The Chancellor's instinct was that option (d) was in principle desirable but that it would be complicated and thus lead to criticism that the Government was creating complexity for its own sake. Indeed, this criticism might also be applied to option (c) which he favoured.

5. The Chief Secretary asked how much effect going beyond option (c) to option (d) would have on the extent to which corporate bonds were used. If option (d) would bring marked benefits then he would be inclined to going ahead with it but not if the gains were marginal and so outweighed by the disadvantages set out in the Financial Secretary's note. Mr Plenderleith did not think that option (c) would cause the corporate bond market to catch fire and he would not claim that option (d) would be very much better. But nevertheless a symmetrical capital treatment for deep discounted bonds would be a perceptible step forward. There was moreover some anecdotal evidence that healthy but non-tax-paying companies might well be attracted by this option. The Bank believedthat it was best to offer as many options as possible and would therefore favour both a symmetrical income treatment on an accruals basis and a symmetrical capital treatment for deep discounted stock. Mr Crawley remarked that it was an open question as to whether maximisation of options was per se an advantage or a disadvantage. It gave individual companies greater choice but on the other hand it could cause confusion and market fragmentation.

6. The Financial Secretary said that it would be possible to introduce the capital route but without going as far as the final option in his paper. He was prepared to drop the proposal to allow the borrower to index his capital "loss" and set it off

against any other capital gains he may have. Mr Beighton said that the Revenue had/ been concerned about this. Pressures would be bound to arise for the indexation of these losses and offsetting them against other capital gains. Once this was conceded it would raise difficult and complicated questions about indexation in the tax system. Mr Crawley added that there has been no great pressure for a capital symmetrical route in the responses to the consultation paper.

7. The Chancellor remained concerned about the complexity introducing both options (c) and (d). Moreover, if one attempted to go for the more limited version of the capital option and not to accept that indexed capital losses should be offsettable against other gains then this would be presented "unfairly" by critics as another example of Ministers succumbing to Revenue pressure. He wondered if it would be a sustainable position. The Financial Secretary argued that the concept of the borrowers' capital loss did not really fit within the normal framework of CGT which was a tax on the increase in the value of assets rather than one's borrowings. Mr Middleton believed that the capital symmetrical route was not complicated and did not run the risks of arbitrage. He supported it provided that capital losses were not to be offset against other gains and this line was sustained. This could then be presented as the equivalent of the capital route already available for indexed stock. The Chief Secretary thought the decision was marginal as could not be sure that many benefits would flow from option (d). But provided that offsetting losses against other gains were not conceded then he argued with the Financial Secretary that the option should be available. Mr Crawley said that whilst there was no direct subsidy in this option it would nevertheless have greater costs than the income symmetrical route because of the greater benefits to the lender.

8. The Chancellor accepted the arguments for introducing both income and capital symmetry for the deep discounted bonds (though without allowing capital losses to be offset against goings elswhere). But he asked about how this could be presented. It was necessary to avoid making it seem so complex as to put off all potential borrowers. Morever, there should be no complicating concessions or further adjustments during the course of the Finance Bill. The first statement of the new tax rules should be definitive and as simple as possible. It might be better to delay in announcing the detail of the decision so that it could be got right. Sir Douglas Wass thought that there were risks in a general announcement on Budget day which could not be supported at the time with a definitive statement of the position. This could cause further confusion. Mr Middleton felt that officials would be able to prepare a Budget Press Notice which was clear enough to serve as the child's guide. The Chancellor concluded in favour of the income and capital symmetrical routes for deep discounted stock (without offsetting capital losses). The details should be announced on Budget Day provided a clear and careful presentation of the decisions was achieved in a Press Notice. The Financial Secretary noted that there was a case for delaying the final decision on (d) until it was seen in worked-up form.

9. In brief discussion the Chancellor agreed that the decision taken at his earlier meeting on Monday, 24 January 1983 against any changes to the tax treatment of gilts in the Budget should stand.

D L Willetts

D L WILLETTS

Circulation:

Those present

Minister of State(R)
Minister of State (C)
Mr Moore
Mr Monck
Mr French

PS/IR

Treasury Chambers
Parliament Street London SW1P 3AG

Telex 262405

Telephone Direct Line 01-233 } 7597
GTN 233 }

Switchboard 01-233 3000

David Keefe Esq (Financial Reporting Unit)
Reuters
85, Fleet Street
LONDON EC4

Your reference

Our reference

Date 2 March 1983

cc Mr Springthorpe, Mrs O'Mara
Mr Haydon
Mr Brazier
Mr Hall
Mr Chandler
Mr Monaghan
Mr Batchelor
Mr Johnson.
Mr Bobrin

Dear David,

Further to my conversation with you this morning and with Peter Knight Barnard yesterday afternoon I confirm that we are prepared to provide you with a page-by-page release of the Chancellor's Budget Speech on Budget Day.

2. George Haydon of this office will be in touch with you shortly to visit you to explain our requirements. As you know these are simply designed to ensure the security of the speech whilst the Chancellor is delivering the speech in the House. George will be accompanied by Nigel Springthorpe who will be responsible on the day for the release arrangements.

3. I would be grateful if you could confirm by letter that this arrangement will remain a confidential one and that no reference will be made to the presence of the Treasury official at Reuters.

4. The procedure on Budget Day is that Mr Springthorpe will bring an unstapled copy of the Chancellor's speech which he will release on a page-by-page basis as he listens to the Chancellor's speech on the radio.

5. Will you please arrange to collect Mr Springthorpe by car from the Treasury on Budget Day. The driver of your car should report to the security guard at the Centre Courtyard of the Treasury, which is entered from King Charles Street. He should have a card with the capital letter R clearly displayed on the windscreen and should park in the centre of the courtyard until he is joined by Mr Springthorpe.

6. Finally could you also please let Mr Haydon here know in advance the registration number of the vehicle and the name of the driver. This information is needed for security purposes to gain access to the Centre Courtyard. Finally we would be grateful if you could return

PERSONAL AND CONFIDENTIAL

Treasury Chambers
Parliament Street London SW1P 3AG

[illegible]

David Keele Esq (Financial Reporter, [illegible])
Reuters
85 Fleet Street
LONDON EC4

2 March 1983

cc [illegible]

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PERSONAL AND CONFIDENTIAL

Nigel to the Treasury from Reuters by car as soon as the Chancellor's speech is over.

7. The car should be here in time to depart for Reuters at 2.45 pm on Budget Day.

Yours Very Truly,

John Page

JOHN PAGE

BUDGET CONFIDENTIAL

cc PS/CST
PS/FST
PS/EST
PS/MST(C)
PS/MST(R)
Mr Middleton
Mr Wicks
Mr Robson
Mr Crawley - IR
PS/IR

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

2 March 1983

The Rt Hon Nigel Lawson
Secretary of State for Energy
Thames House South
Millbank
SW1P 4QJ

Dear Secretary of State,

NORTH SEA FISCAL REGIME

Thank you for your letter of 25 February. You should also have seen the officials' report on onshore and Southern Basin fields. I think we are now in a position to take firm decisions.

We are at one in agreeing that we should be offering the industry an average of £200m or so a year over the next four years. Your main concern has been that the impact of the Consultative Document proposals would prevent our achieving this. We have now looked at the figures for the later years in this period and can reassure you that this will not be so. The average yield from these proposals over this period (even without taking account of the unquantifiable benefits from the new relief system) will be only £10m or so with the ½m tonnes allowance John Wakeham has proposed. (For reasons which could be explained to your people, if you wished, the estimated yield in 85/86 and 86/87 is less than that for 84/85, rather than moving steadily up towards the longer term yield).

Since the average cost of the APRT phasing out proposals in my letter of 21 February, together with appraisal relief, is £212m this means that already the average cost of the oil package as a whole is £200m.

In the light of this I do not think a further relaxation on the general level of throughput allowance proposed for tariffs would be either necessary or appropriate. The ½m tonnes allowance we have proposed is already a generous one. And it is important to remember that an owner field gets this allowance for each user field it takes on, and so can already get 1m tonnes or more in aggregate.

As for agreements made before May 1982, I do not think exemption would be justified either in principle or on the facts. But, following your discussion with John Wakeham, we do think there is a political case for a temporary further abatement. For these existing agreements we therefore propose to increase the abatement to 750,000 tonnes a year

/for

for 5 years only. I understand this would add up to a further £5m a year to the costs I have set out above.

I think these proposals, taken together with the major concessions on PRT oil allowance and royalties for future fields, represent a constructive and generous overall package. I do not however think it would be right to offer the new field reliefs except where they are clearly justified by detailed analysis. On the data available (although I realise this is highly uncertain) neither onshore fields (which I understand you would in any case be happy to exclude) nor Southern Basin fields seem to need extra tax relief. If the industry were unhappy about exclusion we could agree to look at the detailed figures with the operators but we should not in my view take the almost irrevocable step (given the need to preserve the credibility of our future field package generally) of giving expensive new reliefs to fields where no case has yet been made out. I do not believe exclusion need be presentationally damaging.. There is after all no question of making these fields worse off, and they will benefit from APRT phase out and appraisal relief.

Finally, you may like to know that I am proposing to correct an anomaly in 1980 legislation on transfers of interest to which Esso has drawn attention at a cost of £10m in 83/84 (and a yield - the corporation tax consequential - of £5m in 84/85). This will incidentally be presentationally helpful by bringing the total 83/84 cost of the package up to £115 plus. (The costings may of course vary a bit as a result of updating the Budget forecasts.)

If you can agree an overall package on these lines, I would be prepared - as I said in my letter of 21 February - to agree, despite some doubts on the strength of the case, to backdating the new field reliefs to cover N Alwyn and Clyde.

We need to settle all this now, and I hope that you will be able to confirm that you are content with these proposals, which should, I believe, go a long way to meeting the industry's representations, while being manageable - just - in the overall Budgetary context. If you are content, I shall put a summary of the proposals to the Prime Minister this week. If on the other hand we need a further talk, let us meet tomorrow.

Yours ever,

John Kerr

pp GEOFFREY HOWE

approved by the Chancellor, signed in his absence.

BUDGET CONFIDENTIAL

cc PS/CST
PS/FST
PS/EST
PS/MST(C)
PS/MST(R)
Mr Middleton
Mr Wicks
Mr Robson
Mr Crawley - IR
PS/IR

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

2 March 1983

The Rt Hon Nigel Lawson
Secretary of State for Energy
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Millbank
SW1P 4QJ

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Yours ever,

John Kerr

p.p. GEOFFREY HOWE

approved by the Chancellor, signed in his absence.

Ke

Does this cause problems?

M

UNCLASSIFIED

FROM: A W BATCHELOR

DATE: 2 March 1983

MR JOHNSON

cc Miss O'Mara
Mr Brazier
Mr Chambers
Mr Wall
Mr Monaghan
Mr Page
Mr Haydon
Mr Wilkins

BUDGET DOCUMENTATION

Thank you for your minute of 1 March.

2. The figures in Annex A to your minute have been incorporated in the latest version of the Budget Aid Memoire circulated by Miss O'Mara on 28 February. As I explained to you and Mr Page last Friday the total number of snapshots produced is already 13% up on last year. Given the speed with which it is produced as well as our other work I cannot undertake to produce a significant number of extra copies and so I hope you will be able to survive with the number of copies we have already agreed. But having registered the point I realise the importance of ensuring that the press are adequately covered. If I can provide extra copies I will do so but we must rely on you to restrict demand to essentials only.

3. I do not I am afraid control the circulation of the copies listed in Annex B and I must therefore leave Mr Brazier to take this on board.

A W BATCHELOR
27/G
X 7278

FROM: MISS M O'MARA

DATE: 2 March 1983

MR WICKS

cc Chief Secretary
Financial Secretary
Economic Secretary
Minister of State (C)
Minister of State (R)
Sir Douglas Wass
Sir Anthony Rawlinson
Mr Burns
Mr Byatt
Mr Middleton
Mr Burgner
Mr Kemp
Mr Moore

PS/Inland Revenue
PS/Customs & Excise

1983 BUDGET: LETTER FROM SECRETARY OF STATE FOR INDUSTRY OF 25 FEBRUARY

The Chancellor has seen Mr Jenkin's letter of 25 February and would be interested to know the cost of the change described in paragraph 8. But in the light of the Chief Secretary's comments, recorded in Miss Swift's minute of 28 February, he does not think we should stir up the Department of Energy to provide a figure.

MOM

MISS M O'MARA

(PWP)

BUDGET SECRET

FROM: E P KEMP
2 March 1983

PRINCIPAL PRIVATE SECRETARY

cc PS/Chief Secretary
Sir Anthony Rawlinson
Mr Mountfield
Mr Monger

BUDGET COSTS, SOCIAL SECURITY, CHILD BENEFIT AND ALL THAT

I thought it might be helpful if I tried to set out in advance of this afternoon's meeting how, it seems to me, the simple arithmetic involved in the proposals in the Chief Secretary's minute of 1 March, and Mr Monger's minute of 2 March squares with my Table A attached to my overview note of 1 March.

2. I start with paragraph 6 of Mr Monger's minute. This shows costs of the caring package, net, restoration of the 5 per cent abatement, and a £6.50 child benefit (with OPB going up accordingly) of £97 million in 1983-84 and £276 million in 1984-85. The Chief Secretary proposes that this should be offset in part by getting rid of the extension to the Home Improvement Scheme to inter-war houses, which he puts at £25 million but which we have been scoring at £35 million, and by savings on the innovation package. This brings the cost down to £57 million in 1983-84 and £271 million in 1984-85. In my Note A I in fact had been scoring £80 million for 1983-84 and £225 million for 1984-85. Thus we are more for 1983-84, though with a shortfall for 1984-85. However all this is on the basis of taking the child benefit to £6.50. I am advised that if we want to make the claim that we are matching the 1979 level, then a rate of £6.45 (precisely £6.45½) would do. If we moved to £6.45 we save £10 million in 1983-84 and £25 million in 1984-85. Overall, these changes would give us a saving of £33 million on my Note A for 1983-84 at a cost of £21 million for 1984-85. I set out the numbers in tabular form below.

3. The Chancellor and the Chief Secretary may wish to consider the implications of this arithmetic. One point that does emerge is that strictly speaking it is not actually necessary to throw out the extension to the Home Improvement scheme, particularly if its cost is rightly scored at only £25 million; this scheme has the great merit (for this purpose)

of affecting 1983-84 only. On the other hand if the position on the Reserve is tight this points to dropping it, as does the point in Mr Monger's paragra 7 that all this is based on May inflation of $4\frac{1}{4}$ per cent - anything higher has a cost not provided for.

	1983-84		1984-85	
Per Monger:				
Caring, net	1		5	
UB 5 per cent	22		59	
CB £6.50 (+ OPB)	74	97	212	276
Per CST:				
Drop Home Improvements	(35)		-	
Cut Innovation	(5)	(40)	(5)	(5)
Net		57		271
Per Kemp: "Table A"				
Provided for CB - Group A	60		175	
Group B	20	80	50	225
(Excess)/Shortfall		(23)		46
Take CB to £6.45		(10)		(25)
		(33)		21

EPK

E P KEMP

to go through once again the packages tables looking at the ones sidelined, which as far as I can see are largely open, to see what further mopping up can be done this afternoon.

8. Of course a major outstanding point here goes along with the PSBR decisions, namely the money figure ranges we are looking for. We want to confirm finally the figures of 7-11 per cent, 6-10 per cent and 5-9 per cent for 1983-84 to 1985-86 shown in the draft MTFS.

This is my proposal to PK

9. Overall this hangs oil. No doubt this will come up this afternoon. But subject to that, the Chancellor might like to think in terms of a report to the Prime Minister on Thursday evening, which could sweep up most of the outstanding points (including provisional decisions on the PSBR path). It is also worth considering whether the Chancellor wants to let the Prime Minister have sight of the draft Budget Speech over the weekend or whether he wants to wait until next week.

next week

E P KEMP

BUDGET SECRET

FROM: J O KERR

DATE: 3 March 1983

CH/EX REF NO B(83)13

COPY NO 21 OF 22 COPIES

MR KEMP

cc Chief Secretary
Financial Secretary
Economic Secretary
Minister of State (C)
Minister of State (R)
Sir Douglas Wass
Sir Anthony Rawlinson
Mr Burns
Mr Middleton
Mr Bailey
Mr Cassell
Mr Moore
Mr Monger
Mr Mountfield
Mr Ridley
Sir L Airey)
Mr Green) IR
Mr Beightin)

BUDGET DECISIONS ON 3 MARCH: STOP PRESS

This is to confirm to you, and inform copy addressees, that the items outstanding at the end of today's noon meeting have been settled as follows:-

(a) To be included in the Budget

	£m PSBR costs 1983-84	1984-85
Removal of Invalidity Trap	4	14
Widows' Bereavement Allowance Extension	20	25
CTT: increase from (i) 20% to 30% in business relief for minority holdings in unquoted companies and (ii) in agricultural relief for let land	0.5	5
(b) Dropped from the Budget		
ACT carry back, extension to 6 years	-	60

J O KERR

BUDGET SECRET

FROM: JILL RUTTER
DATE: 3 March 1983

PS/FINANCIAL SECRETARY

cc: PS/Chief Secretary
PS/Economic Secretary
PS/Minister of State (C)
PS/Minister of State (R)
Mr Moore
Mr Robson
Mr Aaronson
Mr Haigh- IR
PS/IR

PERSONAL TAXATION: APPROACH TO THE 1983 BUDGET

The Chancellor has seen Mr Haigh's minute of 1 March. He has commented that the figures reveal a grisly tale which has not really come out in the publicity so far.

2. The Chancellor has commented that many people will have had the first news from their notice of coding. He has asked whether that contained an explanation?

3. He will be grateful if the Financial Secretary could consider the adequacy of the whole PR exercise in consultation with the Economic Secretary and the MST(C) in the light of this.

JKR

JILL RUTTER

FROM: J O KERR
DATE: 3 March 1983

MR CRAWLEY - IR

cc: Minister of State (R)
Chief Secretary
Financial Secretary
Economic Secretary
Mr Middleton
Mr Wicks
Mr Robson
Mr Kemp

Sir Lawrence Airey)
Mr Green)
Mr Rogers)
Mr Johns)
PS/IR)

NORTH SEA FISCAL REGIME: MR LAWSON'S FURTHER DEMANDS: YOUR MINUTE OF 3 MARCH

This is to confirm that:-

a. The Minister of State (R) and the Chancellor agreed with your advice, and accepted the concession to Mr Lawson described in your para 1. I conveyed this to the Department of Energy.

b. The Department of Energy withdrew Mr Lawson's second demand, described in your para 4.

c. The Department of Energy did not raise the additional point, on the 1984-85 cost, mentioned in your para 6.

d. The Department of Energy confirmed that Mr Lawson now accepts the deal described in the Chancellor's letter of 2 March, subject to the clarification conceded by us ((a) above).

/e. The Chancellor's

e. The Chancellor's meeting with Mr Lawson tonight was therefore cancelled.

f. The Chancellor will look overnight at your draft report to the Prime Minister, with a view to our agreeing a version of it with Mr Lawson tomorrow, for submission to No 10 tommorrow night.

g. The Department of Energy have agreed to clear with Mr Wicks their reply to the Chancellor's letter of 2 March, which will complete the exchanges recording the deal now struck.

J O KERR

FROM: J O KERR
DATE: 3 March 1983

MR CRAWLEY - IR

cc: Minister of State (R)
Chief Secretary
Financial Secretary
Economic Secretary
Mr Middleton
Mr Wicks
Mr Robson
Mr Kemp

Sir Lawrence Airey)
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J O KERR

M · RAS

BUDGET SECRET

FROM: E P KEMP
3 March 1983

CHANCELLOR OF THE EXCHEQUER

Spread: – Valorise
– 5%

BUDGET STATE OF PLAY

I have sent you notes for the meeting at noon on decisions on the public expenditure elements in the Budget.

2. I have also prepared, and attach, a note showing the overall state of play reflecting yesterday's decisions, the possible public expenditure position depending on decisions to be taken, and the Mortgage Interest Relief position. I am not giving this a wide circulation, but I will have additional copies available if it falls to be discussed this morning.

3. The numbers in it are still a little uncertain, but we are chasing these up and I would like to be able to let you have by end of the day a revised statement with more precise figures and reflecting the decisions on public expenditure, and any other, taken at this morning's meeting. It will also have attached to it the various notes showing the contents of the packages etc; in fact, hopefully it will be a full and near final snapshot of the fiscal side of the Budget. You may find it useful in considering the note which I understand you are thinking of sending to the Prime Minister this evening, a draft of which will be coming forward very shortly..

4. On the figures shown in the table below, you will see that the position has swung around a little in that while for the "total firm" measures 1983-84 at £1550 million is pretty close to the forecasters £1.5 billion for 1984-85 the figure of £1870 is a little less than the forecasters £2 billion. This means that it would be possible to add in the ACT carry-back, which has a 1984-85 cost but not 1983-84. Alternatively it may be desirable to hold the 1984-85 PSBR costs to the lower figure, with a view to buttressing the fiscal adjustment for that year to be shown in the FSBR. And there is still the oil risk.

EPK

E P KEMP

BUDGET SECRET 3 March 1983

BUDGET MEASURES	1983-84 PSBR	1983-84 REVENUE	1984-85 PSBR	1984-85 REVENUE
FIRM				
Tax NIS - ½% from August	200	220	300	400
IT - 8½ over RW + roundings	1010	1170	1060	1490
Specific Duties - net	(10)	(10)	(10)	(10)
Oil - as proposed	105	120	85	100
CT - Package 6(b)	35	40	60	70
MIRC - to £30,000	55	60	70	85
Packages (separate notes)				
Small firms	32	36	132	148
Technology	-	-	10	10
Construction	-	-	15	15
Caring	-	-	4	4
Miscellaneous	3	4	(36)	(42)
Public Expenditure - separate notes	120	250	180	395
TOTAL FIRM	1550	1890	1870	2665
OTHER POSSIBILITIES				
Tax ACT carry back	-	-	60	70
Widows Bereavement	20	25	25	30
Public Expenditure - separate note (say)	~~30~~ 4	30	~~20~~ 14	20
TOTAL POSSIBILITIES	50	55	105	120
GRAND TOTAL	1600	1945	1975	2785
(Grand total of notes of 1 March)	1590	1920	2020	2830)

Scholarships
[illegible] and

FROM: E P KEMP
3 March 1983

CHANCELLOR OF THE EXCHEQUER

cc Chief Secretary
Financial Secretary
Economic Secretary
Minister of State (C)
Minister of State (R)
Sir Douglas Wass
Sir Anthony Rawlinson
Mr Burns
Mr Middleton
Mr Bailey
Mr Cassell
Mr Moore
Mr Monger
Mr Mountfield
~~Mr Pestell~~
~~Mr Hall~~
Mr Ridley
Sir L. Airey
Mr Green
Mr Beighton } IR.

BUDGET - THE PUBLIC EXPENDITURE POSITION

Following the request at your meeting yesterday, we have prepared the tables below which list for decision the public expenditure elements now on the table for the Budget. Category A are the items now favoured, while Category B are some other items which have been in recent lists but which it is now proposed to drop. Costs shown are excesses over the provisions made in the White Paper.

2. All the items adopted will be charged to the Contingency Reserve. This should be stated in the Budget Speech in order to minimise the impression of weakening control and failure to hold to White Paper decisions.

3. For Category A the note below shows not only the gross public expenditure cost but also the net PSBR cost. As advised in previous papers, for 1983-84 the first £100 million of the items charged to the Reserve can be regarded as allowed for in the PSBR forecast; the excess over this scores against fiscal adjustment. For 1984-85 the parallel figure is £175 million. In addition in converting the revenue figures to PSBR figures we have made an allowance for the off-setting saving on benefits arising from the employment measures.

4. I am letting you have separately a total score card for the Budget as it now stands, reflecting the figures shown in the notes below.

5. The figures in the tables below have been agreed with those responsible.

E P KEMP

BUDGET SECRET 3 March 1983

£ million

Category A-Favoured

	1983-84		1984-85	
Social Security				
Raise cut off for SB resources to £3,000	2		7	
Raise cut off for SB single payments to £500	1		3	
Real increase in therapeutic earnings limit	neg		neg	
New mobility supplement for War Pensioners	neg		1	
Less housing benefit savings	(2)		(6)	
Restoration of 5 per cent abatement in UB	22		59	
Increase Child Benefit to £6.50 per week, plus corresponding rise in one parent benefit	74	97	212	276
	L Exum?		L Exum?	
Technology				
As previous package, less £5m reduction on advisory service and computer aids		39		69
Construction				
Enveloping	50		-	
Improvement Grants: uprating cost limits	10	60	10	10
Employment				
DHSS early retirement (automatic credits 2 long-term SB 22)	24		24	
Enterprise allowance; cash limited Nationwide scheme, plus spill over (gross)	25		25	
? Part-time JRS from 62, starting October (gross)	5	54	Note 1 25	49
Gross P/Ex costs		250		394
Less allowed for in PSBR forecast	100		175	
netting of unemployment measures cost	14	114	8	183
		136		211
Less adjustment to PSBR costs		16		31
Net PSBR costs		120		180

Note 1: Unknown - to be determined ad referendum Ministers at D/Em meeting on 3 March

BUDGET SECRET   3 March 1983

	1983-84	1984-85	
Category B - Proposed to drop			
Real increase in Mobility Allowance	2	6	
Removal of Invalidity Trap (net of amount already in Employment package above)	4	14	
Improvement Grant inter-war houses	25	-	
Gross P/Ex costs	29	20	
Summary			
Gross cost of Category A items	250	394	(Note 1)
-ditto- Category B items	29	20	

Note 1: Plus cost of Part-time JRS for 62, still to be determined.

(PWP)

FROM: J O KERR
DATE: 3 March 1983

CH/EX REF NO B(83)13

COPY NO 20 OF 22 COPIES

MR KEMP

cc Chief Secretary
Financial Secretary
Economic Secretary
Minister of State (C)
Minister of State (R)
Sir Douglas Wass
Sir Anthony Rawlinson
Mr Burns
Mr Middleton
Mr Bailey
Mr Cassell
Mr Moore
Mr Monger
Mr Mountfield
Mr Ridley
Sir L Airey)
Mr Green) IR
Mr Beighton)

BUDGET DECISIONS ON 3 MARCH: STOP PRESS

This is to confirm to you, and inform copy addressees, that the items outstanding at the end of today's noon meeting have been settled as follows:-

(a) To be included in the Budget

	£m PSBR costs	
	1983-84	1984-85
Removal of Invalidity Trap	4	14
Widows' Bereavement Allowance Extension	20	25
CTT: increase from (i) 20% to 30% in business relief for minority holdings in unquoted companies and (ii) in agricultural relief for let land	0.5	5
(b) Dropped from the Budget		
ACT carry back, extension to 6 years	-	60

JOK.

J O KERR

CST FST
EST
MST R.
Mr Middleton.
Mr Wicks
Mr Robson.
Mr Kemp.
IR.
Sir. L. Airey
Mr Green
Mr Crawley.
Mr Rogers.
Mr Johns

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

PRIME MINISTER

NORTH SEA FISCAL REGIME

You will wish to know what changes I have in mind for the North Sea fiscal regime in the Budget. They have been fully discussed, and agreed, with Nigel Lawson.

2. My proposals reflect the changed prospects for oil prices. They also benefit from detailed consultations with the industry.

3. Nigel and I have concluded that it is important to concentrate on most cost-effective ways to encourage new development. Existing fields are still, by and large, earning good profits. New fields, by contrast, are likely to be smaller and more complex and therefore generally less profitable.

4. My main proposals are as follows:-

a. First, I intend to help current oil company cash flow, and so give some modest assistance to financing new activity, by phasing out Advance Petroleum Revenue Tax (which advances PRT into the early years of field life) between now and the end of 1986. This has been a major bone of contention with the industry.

b. Second, to encourage exploration and appraisal of new projects, I propose to enable companies to claim immediate PRT relief against any existing field for expenditure after Budget Day on exploration and appraisal.

This would give immediate tax relief worth up to 75p in the £ for such expenditure.

c. Third, and most importantly, for new fields, (which will be defined to include the two N Alwyn and Clyde field, approved within the last year), I propose to double the PRT oil allowance and Nigel Lawson proposes to use his powers to waive royalties. These measures will mean that future fields will pay no special taxes before they have recovered their costs; all taxes will be based on profits; and only corporation tax will be payable on production below 1 million tonnes a year. On the future fields we looked at, this brings the average rate of tax down from over 70 per cent to around 60 per cent.

At this stage we are not extending these reliefs to future onshore or Southern Basin fields because the present evidence suggests that they are likely to be pretty profitable. But I have agreed with Nigel that, so far as Southern Basin fields are concerned, we will be ready to review the position with the industry since the evidence we currently have on their economics is very sparse. If we are convinced that there is a case for extending these concessions to the Southern Basin, we would do so for fields approved for development after Budget Day 1983.

d. Fourth, following last May's consultative document, we would introduce new PRT rules giving full and immediate relief on assets shared between fields (such as pipelines). As a corollary we would bring any related receipts such as pipeline tariffs into charge for PRT. In order to prevent the charge on tariffs discouraging sensible and desirable sharing arrangements for linking in new smaller fields to existing facilities, I am proposing an exemption for the first ½million

tonnes throughput a year for each different user field. This would be increased on a transitional basis to ¾ million tonnes a year for five years for receipts under tariff agreements made before May 1982.

5. These proposals will cost £115 million in 1983/84 and represent a total package of reliefs of over £800 million over the next four years (subject to last minute changes in the forecast). They go a long way to meet the industry's pre-Budget representations, particularly those which they appeared to regard as particularly important.

6. Clearly no tax measures can be guaranteed of themselves to keep up the level of development, particularly at a time when the future of oil prices is so uncertain. And the industry itself recognises that it needs to work on new technological advances to reduce the costs of development of small deep water fields. But I believe these should provide effective, well targeted, fiscal incentives. They go as far as we should - within the overall Budgetary constraints - to meet the industry's concerns.

7. I am copying this to Nigel Lawson.

(G.H.)
4 March 1983

CH/EX REF NO B83\6

COPY NO 10 OF 10 COPIES

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

PRIME MINISTER

THE BUDGET

In this minute I set out the Budget plans, which remain along the lines we have previously discussed. I envisage no major changes - except in the event of a very substantial further fall in the oil price in the next few days.

2. I plan to hold to the figuresfor monetary growth set out in the 1982 Medium Term Financial Strategy - ie ranges of 7-11 per cent for next year, 6-10 per cent for 1984-85 and 5-9 per cent for 1985-86. As before these paths apply to both the narrow and broad measures of money. I hope that we shall hit the middle of the ranges. I have given a good deal of thought to the possibility of reducing at least the top of these ranges by one point. But there is some disadvantage in revising medium term objectives in two successive years. And it is clear that the announcement of a downward move could make it significantly more difficult for us to go on getting interest rates down. In present circumstances, I regard that as decisive.

3. At the time of the last Budget, and again last Autumn, I proposed a figure for the 1983-84 PSBR of 2¾ per cent of GDP, and I plan to hold to this too. For this year (1982-83) we shall publish a forecast out-turn figure of some 3 per cent. The 1984-85 figure, after taking account of the Budget measures and allowing for a future "fiscal adjustment" of £0.5 billion, is forecast at 2½ per cent. Although the nominal figures will coincidentally be £8 billion in all three years, we shall thus continue to show a downward trend as a percentage of GDP.

4. On the basis of the present forecast, an £8 billion PSBR next year gives scope for tax reductions with a PSBR cost of some £1½ billion,

over and above revalorisation of thresholds and excise duties. This figure, however, understates the total reductions we shall have effected for the year 1983-84 because it does not take account of the measures I announced in the Autumn. I shall, of course, ensure (with due discretion) that these are not overlooked.

5. The Annexes below provide a summary of the detailed proposals. Where they have a public expenditure cost it will be accommodated within the Contingency Reserve, and will not lead to any increase in plan totals.

6. As you see, the lion's share of the initial benefit goes to individuals rather than to industry. We both think this is right, given the need to tackle the poverty and unemployment traps, and the way we have favoured industry in previous years, (eg by not increasing thresholds in 1981). Industry is, of course, the main beneficiary of the measures which we announced in the Autumn - and is also helped by the lower exchange rate.

7. The main line of attack on our plans will I think be that we are proposing a "Budget for the Better Off". As you know, I plan to raise all the income tax thresholds and allowances by 8½ per cent over indexation. Using the Government Actuary's earnings assumption of 6½ per cent, this will reduce or match average rates of tax and NIC for 1982-83 for all those contracted-in. But the perceived effect of course is to confer the greatest benefit on the better off and critics will seize on the point that the immediate effect of the Budget changes will be that at fixed levels of income (the so-called static comparison) taking the changes in tax with the NIC increases, married men on salaries of less than £16,000 a year will gain only up to £100 in 1983-84 (and some single people or a few on contracted-out schemes will actually lose.) Yet a married man on £30,000 a year will gain some £600.

8. The increase in the mortgage interest relief ceiling will also give most benefit to the better off. And no doubt our critics will add our plans for social security upratings to their indictment.

9. But there is no sensible way of preventing the perceived effect of increases in the income tax thresholds. One could in theory increase the higher rate bands less than the basic rate thresholds - or even freeze them, as happened over many years in our political youth. But that allows inflation to make the rate structure even more steeply progressive than it already is, and would be wholly wrong. Even if we were to do no more than index the higher rate bands, our £30,000 a year married man would still gain by about £450, and we should scarcely have blunted our opponents' attack. The truth is that all the thresholds and bands suffered similarly from the absence of indexation in 1981; and that all should be corrected now if we are to restore the rate structure - though not yet the levels - set in my 1979 Budget.

10. All this increases the political importance of a number of - not very costly - other measures, viz the increase in child benefit to £6.50, which is above the April 1979 level; the unemployment package we have discussed, together with action on unemployment benefit; extension of the widow's bereavement allowance; removal of the invalidity trap, and so on - the full list is in table 2 of Annex B below. Another useful counter-weight to criticism is the group of minor measures against corporate tax avoidance and fringe benefits listed in table 6 at Annex B.

11. On the positive side, for business and enterprise I am proposing packages of measures to help small and new businesses - including a major simplification and extension of the Business Start-up Scheme, now extended to all existing unquoted companies; new technology - including a £100 million re-introduction of the SEFIS scheme; the construction industry; and wider share ownership. This is all in addition to the further ½ per cent cut in NIS which we discussed some weeks ago: I am sure that it is politically necessary to cope with the "pure" industrial lobby, which has significant backbench support, not least in the West Midlands.

12. I attach at Annex A a summary of the costs of the main proposals. Annex B lists the minor items. You may also wish to glance at the commentary by officials at Annex C.

13. I am sending you a separate note on the oil taxation proposals which I have agreed with Nigel Lawson.

(G.H.)
4 March 1983

£ million

	1983-84 PSBR	1983-84 REVENUE	1984-85 PSBR	1984-85 REVENUE
Individuals				
Personal Allowances	1010	1170	1060	1490
Housing and Home Ownership (Table B1)	80	115	65	105
Social Security (Table B2)	75	125	190	320
Unemployment (Table B3)	25	55	40	75
	1190	1465	1355	1990
Businesses and Industry				
Corporation Tax	35	40	60	70
National Insurance Surcharge	200	220	300	400
Small Firms and Enterprise (Table B4)	25	35	130	165
Technology and Innovation (Table B5)	30	40	50	80
	290	335	540	715
North Sea Oil	105	120	85	100
Specific Duties	(10)	(10)	(10)	(10)
Miscellaneous (Table B6)	-	-	(30)	(45)
GRAND TOTAL	1575	1910	1940	2750

Note 1: The measures include both tax and public expenditure elements. For tax the costs shown are the excess over indexation; for public expenditure the excess over what is already provided in the PEWP.

2: The figures shown are rounded and may still vary marginally. The specific PSBR costs shown for each group of measures is necessarily approximate.

ANNEX B
TABLE 1

HOUSING AND HOME OWNERSHIP

£ million

		1983-84	1984-85	Full Year
1.	Enveloping*	50	nil	-
2.	Mortgage Interest Relief ceiling - increase to £30,000	50	85	60
3.	Improvement grants*	10	10	-
4.	Stock relief: householders part exchange simple scheme	under 1	5	5
5.	Self-employed second home mortgage interest relief	2	5	5
	Revenue costs	52	95	70
	Public expenditure costs	60	10	-
	GRAND TOTAL	112	105	70
	Taken as	115	105	

Note: Items marked * are public expenditure

ANNEX B
TABLE 2

SOCIAL SECURITY

£ million

		1983-84	1984-85
1.	Abolition of £25,000 limit for CTT exemption on gifts to Charities	under 1	under 1
2.	Deeds of Covenant - increase in ceiling for higher rate		3
3.	Tax relief for staff seconded by companies to voluntary bodies	under 1	under 1
4.	Extension of widow's bereavement allowance	25	30
5.	Raise cut-off for SB resources to £3,000 *	2	7
6.	Raise cut-off for SB single payments to £500 *	1	3
7.	Real increase in therapeutic earnings limit *		
8.	New mobility supplement for War Pensioners *		
	Less housing benefit savings	(2)	(6)
9.	Restoration of 5 per cent abatement in UB *	22	59
10.	Increase child benefit to £6.50 per week, plus corresponding rise in one parent benefit *	74	212
11.	Removal of invalidity trap *	4	14
	Revenue costs	25	34
	Public expenditure costs	101	290
	GRAND TOTAL	126	324
	Taken as	125	320

* Public expenditure items. Costs are those over and above amounts provided for in the White Paper

ANNEX B
TABLE 3

UNEMPLOYMENT

£ million

	1983-84	1984-85
DHSS early retirement (automatic credits 2, long-term SB 22)*	24	24
Enterprise allowance: cash limited nationwide scheme, plus spill over (gross)*	25	25
Part-time JRS from 62*	5	25 ≠
GRAND TOTAL	54	74
Taken as	55	75

Note: Items marked * are public expenditure

≠ £25 million is provisional estimate

SMALL FIRMS, ENTERPRISE AND WIDER SHARE OWNERSHIP

£ million

		1983-84	1984-85	Full Year
1.	Business Expansion Scheme	nil	75	75
2.	Loan Guarantee Scheme*	nil	nil	-
3.	Wider share ownership	20	30	40
4.	Capital Gains Tax (see note 1)			
	a. monetary limits	nil	1	1
	b. retirement relief	nil	1	4
5.	VAT registration thresholds	5	10	10
6.	De minimis limit for assessment of apportioned income	under 1	under 1	under 1
7.	Acceptance credits	1	1	1
8.	Capital Transfer Tax (see note 2)	8	18	20
9.	Zero/deep-discounted stock	neg	15	15
10.	Relief for interest, employee buy-outs	1	1	2
11.	Tax treatment of interest paid by companies to non-residents	under 1	under 1	10
12.	Increase in proportion of office space qualifying for industrial building allowance	nil	10	25
13.	DLT - extension of own-use deferment	nil	under 1	4
14.	Small Workshop Scheme - averaging for converted premises	under 1	under 1	under 1
	GRAND TOTAL	36	163	208
	Taken as	35	165	

Note: Items marked * are public expenditure

1. The cost of these CGT measures when statutory indexation is added is nil, 5 and 15 million.

2. Indexation of CTT costs 15, 30 and 45 respectively. The additional costs shown for item 8 are for rounding up the indexed thresholds, for extending the instalment period from 8 to 10 years, and for increasing reliefs on let land and unquoted companies to 30 per cent.

ANNEX B
TABLE 5

TECHNOLOGY AND INNOVATION

£ million

		1983-84	1984-85	1985-86
1.	Extension of transitional period for capital allowances - films	nil	nil	30
2.	Extension of transitional period for capital allowances - teletext TVs	nil	10	15
3.	SEFIS*	20	40	40
4.	Information technology*	5	8	11
5.	Innovation linked investment*	5	15	20
6.	Advisory services*	9	6	6
7.	Science Parks* (included above)			
	Revenue costs	nil	10	45
	Public expenditure costs	39	69	77
	GRAND TOTAL	39	79	122
	Taken as	40	80	

Note: Items marked * are public expenditure

The cost of the whole package over three years is £240 million

ANNEX B

TABLE 6

MISCELLANEOUS

£ million (yields)

		1983-84	1984-85	Full Year
1.	Car and car fuel scales - 15 per cent average increase	nil	(25)	(30)
2.	Cheap housing for directors	nil	nil	(1)
3.	Life assurance: chargeable events: secondhand bonds	under (1)	under (1)	under (1)
4.	CGT: non-resident trusts	under (1)	under (1)	under (1)
5.	CTT: remove special deemed domicile rule for Isle of Man etc	1	2	2
6.	Group relief: avoidance (BL)	nil	(10)	(10)
7.	DLT: disposals by non-residents	(1)	(2)	(2)
8.	Taxation of international business. Offset by Double Taxation Relief against Corporation Tax	nil	nil	nil
9.	Beneficial mortgage loans from employers	nil	under (1)	under (1)
10.	Directors PAYE tax	nil	(10)	(10)
11.	TSBs to be treated as bodies corporate	3	10	10
	GRAND TOTAL	2	(47)	(52)
	Taken as	-	(45)	

Annex C.

INDIVIDUAL MEASURES

Personal Allowances

1. All thresholds and allowances (including the higher rate and IS thresholds) to increase by 14 per cent, or 8½ per cent above the statutory minimum. This will for the great majority of people (but not quite all) more than outweigh the increased National Insurance Contributions which come into effect in April.

Social Security etc.

2. Child benefit to increase to £6.50 per week, taking its value above the level inherited in 1979. There will be a parallel increase in one-parent benefit. The 5 per cent abatement in unemployment benefit, effected in 1980, to be restored; widows bereavement allowance to be extended to a second year; the invalidity trap to be eliminated. Should go some way to offset the criticism on general social security upratings.

Housing and Home Ownership

3. This group includes the increase in the Mortgage Interest Relief ceiling from £25,000 to £30,000. Also included are proposals to provide more for Home Improvement Grants, and also to provide money for so-called "enveloping" schemes, under which local authorities repair the external fabrics of complete streets or terraces, as part of helping counter the problems of housing decay.

Unemployment

4. The measures here include proposals in respect of early retirement, a nationwide extension of the Enterprise Allowance Scheme, and making the Job Release Scheme available to part-timers from the age of 62.

Corporation Tax

5. Reduce the small companies rate from 40 per cent to 38 per cent, and alter the limits so as to reduce the transitional marginal rate.

tional Insurance Surcharge

6. Cut NIS by ½ per cent for the private sector only, from next August. Complete abolition of the Surcharge is the single measure most frequently and forcefully pressed in industrial representations.

Small Firms, Enterprise and Wider Share Ownership

7. A major extension and simplification of the Business Start-Up Scheme, to be called the Business Expansion Scheme. The principal change is the extension of the present scheme to provide tax relief for equity investment not just in new companies but in all qualifying established unquoted trading companies. (Following a review, other changes are being made to make the scheme less restrictive.) Also further measures to encourage wider share ownership, improvements in the Capital Transfer Tax regime, an extension of the Loan Guarantee Scheme, and an increase in the VAT registration threshold.

Technology and Innovation

8. The major measure is the re-opening, at a cost of £100 million over the next three years, of the Small Engineering Firms Investment Scheme (SEFIS). Also included in the total technology package of £240 million over three years is help with Information Technology, Innovation Linked Investment and a provision for extension of Science Parks. It is hoped that this package will particularly benefit the West Midlands.

Other

9. The measures here comprise mainly action on corporate anti-avoidance and personal fringe benefits.

10. On anti-avoidance, the intention is:-

(i) to counter the "British Leyland" device for avoidance through group relief. Treasury Ministers are satisfied that the proposals will not hamper genuine business transactions.

(ii) to legislate on tax havens but not implement the new measures before 1984, and to provide for Double Taxation Relief to be allowed from the same date against the full corporation tax liability before ACT is deducted. This is one of the

changes most widely requested in representations on our corporation tax green paper. Taken together the two changes do not involve any net increase in the burden of tax on international business, but a switch in the burden away from those who remit profits to the UK towards those who accumulate surplus cash balances in tax havens overseas. The tax havens element in the package has been the subject of extensive consultation by Mr Wakeham: he and the Chancellor are satisfied that the proposals in their latest form meet every reasonable representation that has been made during the consultative process.

11. On fringe benefits, the intention is:-

(i) from 1984/85, to increase car and car fuel scales for company cars used privately by higher paid employees by 15 per cent on average. (But the scales will still be well below any realistic estimate of the costs of running a car.)

(ii) on Directors PAYE tax, to deal with cases in which close companies pay directors or higher paid employees a sum without deduction of tax from him and so account for insufficient tax to the Revenue. To do this, tax accounted for by the company will be deemed to be a benefit in kind to the director.

(iii) to tax as a benefit expensive accommodation provided by companies to employees.

(iv) a deficiency in the present rules will be remedied to prevent employees getting both tax relief up to the limit on a commercial mortgage and the benefit of a commensurate interest free loan from the employer for house purchase.

Several other proposals go in the opposite direction:-

(i) the extension from 20 per cent to 30 per cent of the CTT reliefs for minority holdings in unquoted companies, and for let land.

(ii) the removal of the special "deemed domicile" CTT rule applying to those emigrating to the Channel Islands and the Isle of Man. (The Home Secretary has pursued this case for some time.)

(iii) allowing the tenant self-employed (publicans and farmers) to have interest relief on "second" home mortgages.

Specific Duties

12. These will be increased generally in line with inflation, thought with some small real decreases in cigarettes, petrol and derv, and, largely due to rounding, some small real increases in beer, cider and VED. The Chancellor's minute to the Prime Minister of 24 February set out details of the proposals for petrol, derv and VED.

Oil

13. The Chancellor's minute of 4 March reports on the package of measures agreed with the Secretary of State for Energy.

FROM: K BRAZIER
DATE: 4 March 1983

MR JOHNSON

cc Miss M O'Mara
Mr Page
Mr Batchelor

BUDGET DOCUMENTATION

Your minute of 1 March.

Just to confirm that BBC TV will now receive only 1 unstapled/sidelined speech and the extra copy originally allocated to them will now go to the Financial Times Newsroom (via Mr Rowley). Also, the Channel 4 copy of the unstapled/sidelined speech will now go to Reuters at Fleet Street (via Mr Springthorpe).

Finally, the two copies of the unstapled/sidelined speech for PA and Reuters will be handed to Mr Hall by this office before 2.30pm on Budget Day. However, the red side-tagging of these copies has apparently been undertaken by either IDT or EB in recent years and not by the Chancellor's Office.

K Brazier

K BRAZIER

FROM: K BRAZIER

DATE: 4 March 1983

MR JOHNSON

cc Miss M O'Mara
Mr Page
Mr Batchelor

BUDGET DOCUMENTATION

Your minute of 1 March.

Just to confirm that BBC TV will now receive only 1 unstapled/sidelined speech and the extra copy originally allocated to them will now go to the Financial Times Newsroom (via Mr Rowley). Also, the Channel 4 copy of the unstapled/sidelined speech will now go to Reuters at Fleet Street (via Mr Springthorpe).

Finally, the two copies of the unstapled/sidelined speech for PA and Reuters will be handed to Mr Hall by this office before 2.30pm on Budget Day. However, the red side-tagging of these copies has apparently been undertaken by either IDT or EB in recent years and not by the Chancellor's Office.

K Brazier

K BRAZIER

FROM: A. M. BAILEY
4th March, 1983.

CONFIDENTIAL

MR. KEMP

c.c. Mr. R. I. G. Allen
Mr. Norgrove
Mr. Gordon

BUDGET 1983 - BRIEFING THE CBI

Mr. Allen's minute of 3rd March asks for my views:

(i) I think we should provide CBI again with an aide-memoire this year; Mr. Allen may well be right that it has to be defensive and (mildly) propagandist, but it is helpful to them in providing quick reactions, and they are already asking about it, so it would be counter-productive to refuse - and it may well help the early reception (bringing out the 'Autumn plus Budget' totals, showing the breadth of measures for industry, and getting the summary details straight).

(ii) It would be helpful if EB could prepare it, but no doubt IA could find the resources if necessary (and if they can be cleared on "need to know" grounds). Pace Mr. Andren, I see no need to clear this specifically with the Chancellor - Private Office are aware of the proposal to repeat last year's arrangements and indeed are pressing us to nominate someone to take charge of the mechanics. So could EB and IA sort out who will do what?

(iii) I do not myself see the same need to make arrangements for TUC or NEDO - the latter will not be asked for immediate comments, and the former will be hostile anyway.

AMB

A. M. BAILEY

Mr Kemp

I have agreed with Mr Gordon that we (EB) will have a go at it, in consultation with IA.

RA 4/3

cc PPS
Mr Bailey
Mr P. Gordon

~~Mott~~ to see
PWP

CH/EX REF NO B83/6

COPY NO 7 OF 7 COPIES

(PWP)

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

PRIME MINISTER

THE BUDGET

In this minute I set out the Budget plans, which remain along the lines we have previously discussed. I envisage no major changes - except in the event of a very substantial further fall in the oil price in the next few days.

2. I plan to hold to the figures for monetary growth set out in the 1982 Medium Term Financial Strategy - ie ranges of 7-11 per cent for next year, 6-10 per cent for 1984-85 and 5-9 per cent for 1985-86. As before these paths apply to both the narrow and broad measures of money. I hope that we shall hit the middle of the ranges. I have given a good deal of thought to the possibility of reducing at least the top of these ranges by one point. But there is some disadvantage in revising medium term objectives in two successive years. And it is clear that the announcement of a downward move could make it significantly more difficult for us to go on getting interest rates down. In present circumstances, I regard that as decisive.

3. At the time of the last Budget, and again last Autumn, I proposed a figure for the 1983-84 PSBR of 2¾ per cent of GDP, and I plan to hold to this too. For this year (1982-83) we shall publish a forecast out-turn figure of some ~~3~~ 2¾ per cent. The 1984-85 figure, after taking account of the Budget measures and allowing for a future "fiscal adjustment" of £0.5 billion, is forecast at 2½ per cent. ~~Although the nominal figures will coincidentally be £8 billion in all three years, we shall thus continue to show a downward trend as a percentage of GDP.~~

Now 82/3 7½ 2¾ 83/4 8 2¾ 84/5 8 2½ (+ f.a. of ½) 85/6 7½ (f.a. of 4)

4. On the basis of the present forecast, an £8 billion PSBR next year gives scope for tax reductions with a PSBR cost of some £1½ billion,

over and above revalorisation of thresholds and excise duties. This figure, however, understates the total reductions we shall have effected for the year 1983-84 because it does not take account of the measures I announced in the Autumn. I shall, of course, ensure (with due discretion) that these are not overlooked.

5. The Annexes below provide a summary of the detailed proposals. Where they have a public expenditure cost it will be accommodated within the Contingency Reserve, and will not lead to any increase in plan totals.

6. As you see, the lion's share of the initial benefit goes to individuals rather than to industry. We both think this is right, given the need to tackle the poverty and unemployment traps, and the way we have favoured industry in previous years, (eg by not increasing thresholds in 1981). Industry is, of course, the main beneficiary of the measures which we announced in the Autumn - and is also helped by the lower exchange rate.

7. The main line of attack on our plans will I think be that we are proposing a "Budget for the Better Off". As you know, I plan to raise <u>all</u> the income tax thresholds and allowances by 8½ per cent over indexation. Using the Government Actuary's earnings assumption of 6½ per cent, this will reduce or match average rates of tax and NIC for 1982-83 for all those contracted-in. But the perceived effect of course is to confer the greatest benefit on the better off and critics will seize on the point that the immediate effect of the Budget changes will be that at fixed levels of income (the so-called static comparison) taking the changes in tax with the NIC increases, married men on salaries of less than £16,000 a year will gain only up to £100 in 1983-84 (and some single people or a few on contracted-out schemes will actually lose.) Yet a married man on £30,000 a year will gain some £600.

8. The increase in the mortgage interest relief ceiling will also give most benefit to the better off. And no doubt our critics will add our plans for social security upratings to their indictment.

9. But there is no sensible way of preventing the perceived effect of increases in the income tax thresholds. One could in theory increase the higher rate bands less than the basic rate thresholds - or even freeze them, as happened over many years in our political youth. But that allows inflation to make the rate structure even more steeply progressive than it already is, and would be wholly wrong. Even if we were to do no more than index the higher rate bands, our £30,000 a year married man would still gain by about £450, and we should scarcely have blunted our opponents' attack. The truth is that <u>all</u> the thresholds and bands suffered similarly from the absence of indexation in 1981; and that <u>all</u> should be corrected now if we are to restore the rate structure - though not yet the levels - set in my 1979 Budget.

10. All this increases the political importance of a number of - not very costly - other measures, viz the increase in child benefit to £6.50, which is above the April 1979 level; the unemployment package we have discussed, together with action on unemployment benefit; extension of the widow's bereavement allowance; removal of the invalidity trap, and so on - the full list is in table 2 of Annex B below. Another useful counter-weight to criticism is the group of minor measures against corporate tax avoidance and fringe benefits listed in table 6 at Annex B.

11. On the positive side, for business and enterprise I am proposing packages of measures to help small and new businesses - including a major simplification and extension of the Business Start-up Scheme, now extended to all existing unquoted companies; new technology - including a £100 million re-introduction of the SEFIS scheme; the construction industry; and wider share ownership. This is all in addition to the further ½ per cent cut in NIS which we discussed some weeks ago: I am sure that it is politically necessary to cope with the "pure" industrial lobby, which has significant backbench support, not least in the West Midlands.

... 12. I attach at Annex A a summary of the costs of the main proposals. Annex B lists the minor items. You may also wish to glance at the commentary by officials at Annex C.

13. I am sending you a separate note on the oil taxation proposals which I have agreed with Nigel Lawson.

(G.H.)
4 March 1983

NB - overtaken
see new tables.

ANNEX A

£ million

	1983-84 PSBR	1983-84 REVENUE	1984-85 PSBR	1984-85 REVENUE
Individuals				
Personal Allowances	1010	1170	1060	1490
Housing and Home Ownership (Table B1)	80	115	65	105
Social Security (Table B2)	75	125	190	320
Unemployment (Table B3)	25	55	40	75
	1190	1465	1355	1990
Businesses and Industry				
Corporation Tax	35	40	60	70
National Insurance Surcharge	200	220	300	400
Small Firms and Enterprise (Table B4)	25	35	130	165
Technology and Innovation (Table B5)	30	40	50	80
	290	335	540	715
North Sea Oil	105	120	85	100
Specific Duties	(10)	(10)	(10)	(10)
Miscellaneous (Table B6)	-	-	(30)	(45)
GRAND TOTAL	1575	1910	1940	2750

Note 1: The measures include both tax and public expenditure elements. For tax the costs shown are the excess over indexation; for public expenditure the excess over what is already provided in the PEWP.

2: The figures shown are rounded and may still vary marginally. The specific PSBR costs shown for each group of measures is necessarily approximate.

ANNEX B

TABLE 1

HOUSING AND HOME OWNERSHIP

£ million

	1983-84	1984-85	Full Year
1. Enveloping*	50	nil	-
2. Mortgage Interest Relief ceiling - increase to £30,000	50	85	60
3. Improvement grants*	10	10	-
4. Stock relief: householders part exchange simple scheme	under 1	5	5
5. Self-employed second home mortgage interest relief	2	5	5
Revenue costs	52	95	70
Public expenditure costs	60	10	-
GRAND TOTAL	112	105	70
Taken as	115	105	

Note: Items marked * are public expenditure

ANNEX B
TABLE 2

SOCIAL SECURITY

		£ million	
		1983-84	1984-85
1.	Abolition of £25,000 limit for CTT exemption on gifts to Charities	under 1	under 1
2.	Deeds of Covenant - increase in ceiling for higher rate		3
3.	Tax relief for staff seconded by companies to voluntary bodies	under 1	under 1
4.	Extension of widow's bereavement allowance	25	30
5.	Raise cut-off for SB resources to £3,000 *	2	7
6.	Raise cut-off for SB single payments to £500 *	1	3
7.	Real increase in therapeutic earnings limit *		
8.	New mobility supplement for War Pensioners *		
	Less housing benefit savings	(2)	(6)
9.	Restoration of 5 per cent abatement in UB *	22	59
10.	Increase child benefit to £6.50 per week, plus corresponding rise in one parent benefit *	74	212
11.	Removal of invalidity trap *	4	14
	Revenue costs	25	34
	Public expenditure costs	101	290
	GRAND TOTAL	126	324
	Taken as	125	320

* Public expenditure items. Costs are those over and above amounts provided for in the White Paper

ANNEX B

TABLE 3

UNEMPLOYMENT

£ million

	1983-84	1984-85
DHSS early retirement (automatic credits 2, long-term SB 22)*	24	24
Enterprise allowance: cash limited nationwide scheme, plus spill over (gross)*	25	25
Part-time JRS from 62*	5	25 ≠
GRAND TOTAL	54	74
Taken as	55	75

Note: Items marked * are public expenditure

≠ £25 million is provisional estimate

ANNEX B

TABLE 4

SMALL FIRMS, ENTERPRISE AND WIDER SHARE OWNERSHIP

£ million

		1983-84	1984-85	Full Year
1.	Business Expansion Scheme	nil	75	75
2.	Loan Guarantee Scheme*	nil	nil	-
3.	Wider share ownership	20	30	40
4.	Capital Gains Tax (see note 1)			
	a. monetary limits	nil	1	1
	b. retirement relief	nil	1	4
5.	VAT registration thresholds	5	10	10
6.	De minimis limit for assessment of apportioned income	under 1	under 1	under 1
7.	Acceptance credits	1	1	1
8.	Capital Transfer Tax (see note 2)	8	18	20
9.	Zero/deep-discounted stock	neg	15	15
10.	Relief for interest, employee buy-outs	1	1	2
11.	Tax treatment of interest paid by companies to non-residents	under 1	under 1	10
12.	Increase in proportion of office space qualifying for industrial building allowance	nil	10	25
13.	DLT - extension of own-use deferment	nil	under 1	4
14.	Small Workshop Scheme - averaging for converted premises	under 1	under 1	under 1
	GRAND TOTAL	36	163	208
	Taken as	35	165	

Note: Items marked * are public expenditure

1. The cost of these CGT measures when statutory indexation is added is nil, 5 and 15 million.

2. Indexation of CTT costs 15, 30 and 45 respectively. The additional costs shown for item 8 are for rounding up the indexed thresholds, for extending the instalment period from 8 to 10 years, and for increasing reliefs on let land and unquoted companies to 30 per cent.

ANNEX B
TABLE 5

TECHNOLOGY AND INNOVATION

£ million

		1983-84	1984-85	1985-86
1.	Extension of transitional period for capital allowances - films	nil	nil	30
2.	Extension of transitional period for capital allowances - teletext TVs	nil	10	15
3.	SEFIS*	20	40	40
4.	Information technology*	5	8	11
5.	Innovation linked investment*	5	15	20
6.	Advisory services*	9	6	6
7.	Science Parks* (included above)			
	Revenue costs	nil	10	45
	Public expenditure costs	39	69	77
	GRAND TOTAL	39	79	122
	Taken as	40	80	

Note: Items marked * are public expenditure

The cost of the whole package over three years is £240 million

ANNEX B

TABLE 6

MISCELLANEOUS

£ million (yields)

		1983-84	1984-85	Full Year
1.	Car and car fuel scales - 15 per cent average increase	nil	(25)	(30)
2.	Cheap housing for directors	nil	nil	(1)
3.	Life assurance: chargeable events: secondhand bonds	under (1)	under (1)	under (1)
4.	CGT: non-resident trusts	under (1)	under (1)	under (1)
5.	CTT: remove special deemed domicile rule for Isle of Man etc	1	2	2
6.	Group relief: avoidance (BL)	nil	(10)	(10)
7.	DLT: disposals by non-residents	(1)	(2)	(2)
8.	Taxation of international business. Offset by Double Taxation Relief against Corporation Tax	nil	nil	nil
9.	Beneficial mortgage loans from employers	nil	under (1)	under (1)
10.	Directors PAYE tax	nil	(10)	(10)
11.	TSBs to be treated as bodies corporate	3	10	10
	GRAND TOTAL	2	(47)	(52)
	Taken as	-	(45)	

Annex C.

INDIVIDUAL MEASURES

Personal Allowances

1. All thresholds and allowances (including the higher rate and IS thresholds) to increase by 14 per cent, or 8½ per cent above the statutory minimum. This will for the great majority of people (but not quite all) more than outweigh the increased National Insurance Contributions which come into effect in April.

Social Security etc.

2. Child benefit to increase to £6.50 per week, taking its value above the level inherited in 1979. There will be a parallel increase in one-parent benefit. The 5 per cent abatement in unemployment benefit, effected in 1980, to be restored; widows bereavement allowance to be extended to a second year; the invalidity trap to be eliminated. Should go some way to offset the criticism on general social security upratings.

Housing and Home Ownership

3. This group includes the increase in the Mortgage Interest Relief ceiling from £25,000 to £30,000. Also included are proposals to provide more for Home Improvement Grants, and also to provide money for so-called "enveloping" schemes, under which local authorities repair the external fabrics of complete streets or terraces, as part of helping counter the problems of housing decay.

Unemployment

4. The measures here include proposals in respect of early retirement, a nationwide extension of the Enterprise Allowance Scheme, and making the Job Release Scheme available to part-timers from the age of 62.

Corporation Tax

5. Reduce the small companies rate from 40 per cent to 38 per cent, and alter the limits so as to reduce the transitional marginal rate.

National Insurance Surcharge

6. Cut NIS by ½ per cent for the private sector only, from next August. Complete abolition of the Surcharge is the single measure most frequently and forcefully pressed in industrial representations.

Small Firms, Enterprise and Wider Share Ownership

7. A major extension and simplification of the Business Start-Up Scheme, to be called the Business Expansion Scheme. The principal change is the extension of the present scheme to provide tax relief for equity investment not just in new companies but in all qualifying established unquoted trading companies. (Following a review, other changes are being made to make the scheme less restrictive.) Also further measures to encourage wider share ownership, improvements in the Capital Transfer Tax regime, an extension of the Loan Guarantee Scheme, and an increase in the VAT registration threshold.

Technology and Innovation

8. The major measure is the re-opening, at a cost of £100 million over the next three years, of the Small Engineering Firms Investment Scheme (SEFIS). Also included in the total technology package of £240 million over three years is help with Information Technology, Innovation Linked Investment and a provision for extension of Science Parks. It is hoped that this package will particularly benefit the West Midlands.

Other

9. The measures here comprise mainly action on corporate anti-avoidance and personal fringe benefits.

10. On anti-avoidance, the intention is:-

(i) to counter the "British Leyland" device for avoidance through group relief. Treasury Ministers are satisfied that the proposals will not hamper genuine business transactions.

(ii) to legislate on tax havens but not implement the new measures before 1984, and to provide for Double Taxation Relief to be allowed from the same date against the full corporation tax liability before ACT is deducted. This is one of the

changes most widely requested in representations on our corporation tax green paper. Taken together the two changes do not involve any net increase in the burden of tax on international business, but a switch in the burden away from those who remit profits to the UK towards those who accumulate surplus cash balances in tax havens overseas. The tax havens element in the package has been the subject of extensive consultation by Mr Wakeham: he and the Chancellor are satisfied that the proposals in their latest form meet every reasonable representation that has been made during the consultative process.

11. On fringe benefits, the intention is:-

(i) from 1984/85, to increase car and car fuel scales for company cars used privately by higher paid employees by 15 per cent on average. (But the scales will still be well below any realistic estimate of the costs of running a car.)

(ii) on Directors PAYE tax, to deal with cases in which close companies pay directors or higher paid employees a sum without deduction of tax from him and so account for insufficient tax to the Revenue. To do this, tax accounted for by the company will be deemed to be a benefit in kind to the director.

(iii) to tax as a benefit expensive accommodation provided by companies to employees.

(iv) a deficiency in the present rules will be remedied to prevent employees getting both tax relief up to the limit on a commercial mortgage and the benefit of a commensurate interest free loan from the employer for house purchase.

Several other proposals go in the opposite direction:-

(i) the extension from 20 per cent to 30 per cent of the CTT reliefs for minority holdings in unquoted companies, and for let land.

(ii) the removal of the special "deemed domicile" CTT rule applying to those emigrating to the Channel Islands and the Isle of Man. (The Home Secretary has pursued this case for some time.)

(iii) allowing the tenant self-employed (publicans and farmers) to have interest relief on "second" home mortgages.

Specific Duties

12. These will be increased generally in line with inflation, thought with some small real decreases in cigarettes, petrol and derv, and, largely due to rounding, some small real increases in beer, cider and VED. The Chancellor's minute to the Prime Minister of 24 February set out details of the proposals for petrol, derv and VED.

Oil

13. The Chancellor's minute of 4 March reports on the package of measures agreed with the Secretary of State for Energy.

SECRET

PMP

From: Sir A Rawlinson
Date: 4 March 1983

CHANCELLOR OF THE EXCHEQUER

cc Chief Secretary
Sir Douglas Wass
Mr Burns
Mr Middleton
Mr Byatt
Mr Littler
Mr Bailey
Mr Mountfield
Mr Cassell
Mr Kemp

BUDGET: PUBLIC EXPENDITURE CUTS TO OFFSET LOWER OIL PRICES

As requested at your meeting this morning I submit a note on this subject.

2. I must confirm that there is little to be considered at this stage on the public expenditure front for 1983-84.

3. The first priority for cuts must be some or all of the new additions to programmes being announced in the Budget. But you would have to get the agreement of the Ministers concerned, and the case in favour of each of these items, which has been accepted so far, still stands.

4. My own feeling is that the savings which might feasibly be picked up here are hardly worth the disadvantages of losing the items concerned from the Budget.

Lets see if the storm really blows

AKR

A K RAWLINSON

BUDGET: REDUCING PUBLIC EXPENDITURE TO OFFSET LOWER OIL PRICES

This note considers the scope for action on public expenditure to offset an increase in the PSBR resulting from lower oil prices. The assumption is that the gap to be filled is of the order of say £0.5bn.

2. This note is concerned solely with 1983-84. For the later years the question of public expenditure adjustments will be part of the next Survey.

3. The contingency contemplated means crudely that the scope for fiscal adjustment in the Budget is £0.5bn less than previously predicted. The natural response is to reconsider decisions not yet announced which were to contribute to the fiscal adjustment proposed in the Budget.

4. On the expenditure side the following are the Budget measures in this category:

	£m	
Construction: enveloping	50	
uprating improvement grants cost limits	10	
Technology and innovation:		
SEFIS	20	
Other	19	
Employment:		
Early retirement	23	
Enterprise allowance	25 gross)	16 net
Part time JRS from 62	5 gross)	
Social security:		
Child benefit (£6.50)	74 (£6.40 saves 20)	
Restoration of 5% UB	22	
SB, net of HB savings	2	
Removing invalidity trap	4	
	254 (gross)	

5. Excluded from this list is the social security general uprating. The decisions taken here could hardly be reopened now.

6. On child benefit £6.40 rather than £6.50 would save £20m.

7. Any or all of the other items could be dropped entirely, subject to agreement with the spending Minister concerned. If all were dropped, and child benefit at £6.40, the saving would be about £185m (the employment measures being scored net). If some are retained, the saving will be that much less.

8. If savings are decided on, it is for consideration whether to announce reduction of the Contingency Reserve by a similar amount. This would reduce the planning total. It would not add to the savings, since it would reduce shortfall. Provided that the Reserve were not breached, it would ensure that the predicted shortfall is not taken up by other decisions later. The risk, already present but accepted, of breaching the Reserve would be unchanged, provided that the reduction is no more than the bids now being dropped.

9. If the savings decided on justify it, it would be worthwhile reducing the Reserve by say £100m or £150m as appropriate. It may look fiddly, but it will help to ensure that the savings occur.

10. The above are the first priorities for savings. To go further by seeking savings by reopening the White Paper programme decisions can only come into consideration if Ministers declare a crisis and collectively agree to pursue crash cuts over all or most of the programmes. This cannot be recommended: disruptive, wasteful, bad management, and no chance of collective agreement in time for the Budget.

11. Also not recommended are specific cuts limited to programmes where oil prices are important, eg Defence, NHS and to a lesser extent PSA. It has been recognised that major changes in prices, especially in prices generally, may call for some adjustment of cash programmes in either direction, but adjustments for particular prices during the year are contrary to the principles of cash planning and cash limits. To seek a downward adjustment now because of lower oil prices would invite counter-claims for additions later to meet increases in other costs, eg lower exchange rates (the Estimates were done on the November rate) or pay settlements over 3½%, and be a move back towards volume planning and entitlements. In the case of Defence, there is already an important additional cost on account of the fall in the exchange rate which has occurred so far.

12. If, contrary to these recommendations, crash cuts were sought, it is likely that most of what might be agreed at short notice would be surrender of what will on present form be shortfall; and so not properly scored as saving.

13. Effects of lower oil prices on nationalised industries were discussed in the Department of Energy paper annexed to Mr Middleton's note of 1 March.

4 March 1983

FROM: F CASSELL
DATE: 4 March 1983

CHANCELLOR OF THE EXCHEQUER

cc Chief Secretary
Sir Douglas Wass
Sir Anthony Rawlinson
Mr Burns
Mr Littler
Mr Middleton
Mr Kemp
Mr Moore

At your meeting this morning you asked us to think about contingency plans as to how the Budget might be amended if the oil price fell below what is now assumed between now and, say, the afternoon of Monday 14 March!

2. There was general agreement at your meeting that:

- fall of up to $2 a barrel in the North Sea price (to $28.50) could probably be accommodated without significant changes to the Industry Act forecast or MTFS.

- this would imply that no change to the Budget would be called for so long as the world oil price (Saudi Arabian Light crude) did not fall below $27.

- any larger fall (unless it were thought to be only very temporary) would probably require some reduction in the Budget package, to keep the PSBR within reasonable bounds.

- though everything is highly uncertain, the likelihood is that oil prices will not fall very substantially in the coming week. $25 looks to be a reasonable estimate of the lower end of the range of risk.

3. The table below gives our best estimates of the effects on the PSBR of a fall in the world oil price to respectively $27, $26 and $25.

EFFECTS ON PSBR £ billion

World Oil Price	1983-84		1984-85
$27	0.5		0.7
$26	0.9	·8 bn	1.2
$25	$\boxed{1.3}$		1.8

These estimates assume that the monetary guidelines are held to and that the exchange rate falls only modestly - as implied by the relationships in the Treasury model, but a major uncertainty. If the exchange rate fell by more, the damage to the PSBR would be less, but the need for taking offsetting action might be greater on other grounds.

4. Since the fall in the oil price would (by reducing inflation and improving the financial position of companies) reduce the private sector's demand for credit some increase in the PSBR could certainly be accommodated without endangering monetary policy. So it would not be necessary to take action to restore the whole of the PSBR loss. What proportion could be absorbed would have to be judged in the light of all the circumstances, including of course the reactions of financial markets.

5. If the fall occurred between now and the Budget quick and bold action would be needed. To trek again over the whole range of small measures in the Budget would not measure up to the needs of the situation. Action would have to be taken on one or more of the big items in the Budget. There are six costing over £50 million in 1983-84:

NIS	-	PSBR cost	200
Personal allowances	-		1010
MIRC	-		55
Oil	-		105
Child benefit	-		75 ?
Enveloping	-		50

In addition, an increase in petrol and derv duties (over and above indexation) could be considered - though as pointed out at this morning's meeting the case for this on its merits would not be strong. A 10p increase in these duties would reduce the PSBR by £450 million in 1983-84.

6. Looking at the above list, NIS would be the most obvious candidate for ditching, given the further improvement in company finances that lower oil prices would bring. The oil package would be very difficult to drop in this situation. On personal allowances there would be a range of options - for illustration a reduction of 1 point would improve the PSBR by about £120 million in 1983-84. Each 10p off CB is worth about £20m.

7. If oil prices fell after the Budget then the arguments put forward in my submission of 11 February would apply. Briefly, if early fiscal action were required it would probably have to take the form of higher indirect taxes. The present regulator powers seem fully adequate to produce revenues on the scale needed - these allow excise duties to be varied, selectively or across the board, by up to 10 per cent and the VAT rate to be changed by up to $3\frac{3}{4}$ points in either direction. Fully used from the beginning of the financial year, the excise duty regulator could raise about £1 billion of revenue in 1983-84 and the VAT regulator about £$2\frac{1}{2}$ billion. On a longer view, it would be desirable, assuming the lower oil price looked likely to be "permanent", to make good part of the PSBR loss by reducing public expenditure. Sir Anthony Rawlinson is putting in a separate submission

on this. It is difficult to see much being achieved by this route in the short-term.

8. We can elaborate on some of these options in more detail next week. But I hope this note gives some idea of the possible size of the problem and of the kind of options available.

F CASSELL

1.37

SECRET

From: Sir A Rawlinson
Date: 4 March 1983

CHANCELLOR OF THE EXCHEQUER

cc Chief Secretary
Sir Douglas Wass
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uprating improvement grants cost limits	10	
Technology and innovation:		
SEFIS	20	
Other	19	
Employment:		
Early retirement	23	
Enterprise allowance	25 gross)	16 net
Part time JRS from 62	5 gross)	
Social security:		
Child benefit (£6.50)	74 (£6.40 saves 20)	
Restoration of 5% UB	22	
SB, net of HB savings	2	
Removing invalidity trap	4	
	254 (gross)	

5. Excluded from this list is the social security general uprating. The decisions taken here could hardly be reopened now.

6. On child benefit £6.40 rather than £6.50 would save £20m.

.. Any or all of the other items could be dropped entirely, subject to agreement with the spending Minister concerned. If all were dropped, and child benefit at £6.40, the saving would be about £185m (the employment measures being scored net). If some are retained, the saving will be that much less.

8. If savings are decided on, it is for consideration whether to announce reduction of the Contingency Reserve by a similar amount. This would reduce the planning total. It would not add to the savings, since it would reduce shortfall. Provided that the Reserve were not breached, it would ensure that the predicted shortfall is not taken up by other decisions later. The risk, already present but accepted, of breaching the Reserve would be unchanged, provided that the reduction is no more than the bids now being dropped.

9. If the savings decided on justify it, it would be worthwhile reducing the Reserve by say £100m or £150m as appropriate. It may look fiddly, but it will help to ensure that the savings occur.

10. The above are the first priorities for savings. To go further by seeking savings by reopening the White Paper programme decisions can only come into consideration if Ministers declare a crisis and collectively agree to pursue crash cuts over all or most of the programmes. This cannot be recommended: disruptive, wasteful, bad management, and no chance of collective agreement in time for the Budget.

11. Also not recommended are specific cuts limited to programmes where oil prices are important, eg Defence, NHS and to a lesser extent PSA. It has been recognised that major changes in prices, especially in prices generally, may call for some adjustment of cash programmes in either direction, but adjustments for particular prices during the year are contrary to the principles of cash planning and cash limits. To seek a downward adjustment now because of lower oil prices would invite counter-claims for additions later to meet increases in other costs, eg lower exchange rates (the Estimates were done on the November rate) or pay settlements over 3½%, and be a move back towards volume planning and entitlements. In the case of Defence, there is already an important additional cost on account of the fall in the exchange rate which has occurred so far.

12. If, contrary to these recommendations, crash cuts were sought, it is likely that most of what might be agreed at short notice would be surrender of what will on present form be shortfall; and so not properly scored as saving.

13. Effects of lower oil prices on nationalised industries were discussed in the Department of Energy paper annexed to Mr Middleton's note of 1 March.

4 March 1983

FROM: F CASSELL
DATE: 4 March 1983

CHANCELLOR OF THE EXCHEQUER

cc Chief Secretary
Sir Douglas Wass
Sir Anthony Rawlinson
Mr Burns
Mr Littler
Mr Middleton
Mr Kemp
Mr Moore

At your meeting this morning you asked us to think about contingency plans as to how the Budget might be amended if the oil price fell below what is now assumed between now and, say, the afternoon of Monday 14 March!

2. There was general agreement at your meeting that:

- fall of up to $2 a barrel in the North Sea price (to $28.50) could probably be accommodated without significant changes to the Industry Act forecast or MTFS.

- this would imply that no change to the Budget would be called for so long as the world oil price (Saudi Arabian Light crude) did not fall below $27.

- any larger fall (unless it were thought to be only very temporary) would probably require some reduction in the Budget package, to keep the PSBR within reasonable bounds.

- though everything is highly uncertain, the likelihood is that oil prices will not fall very substantially in the coming week $25 looks to be a reasonable estimate of the lower end of the range of risk.

3. The table below gives our best estimates of the effects on the PSBR of a fall in the world oil price to respectively $27, $26 and $25.

EFFECTS ON PSBR £ billion

World Oil Price	1983-84	1984-85
$27	0.5	0.7
$26	0.9	1.2
$25	1.3	1.8

These estimates assume that the monetary guidelines are held to and that the exchange rate falls only modestly - as implied by the relationships in the Treasury model, but a major uncertainty. If the exchange rate fell by more, the damage to the PSBR would be less, but the need for taking offsetting action might be greater on other grounds.

4. Since the fall in the oil price would (by reducing inflation and improving the financial position of companies) reduce the private sector's demand for credit some increase in the PSBR could certainly be accommodated without endangering monetary policy. So it would not be necessary to take action to restore the whole of the PSBR loss. What proportion could be absorbed would have to be judged in the light of all the circumstances, including of course the reactions of financial markets.

5. <u>If the fall occurred between now and the Budget</u> quick and bold action would be needed. To trek again over the whole range of small measures in the Budget would not measure up to the needs of the situation. Action would have to be taken on one or more of the big items in the Budget. There are six costing over £50 million in 1983-84:

NIS	-	PSBR cost	200
Personal allowances	-		1010
MIRC	-		55
Oil	-		105
Child benefit	-		75
Enveloping	-		50

In addition, an increase in petrol and derv duties (over and above indexation) could be considered - though as pointed out at this morning's meeting the case for this on its merits would not be strong. A 10p increase in these duties would reduce the PSBR by £450 million in 1983-84.

6. Looking at the above list, NIS would be the most obvious candidate for ditching, given the further improvement in company financ that lower oil prices would bring. The oil package would be very difficult to drop in this situation. On personal allowances there would be a range of options - for illustration a reduction of 1 point would improve the PSBR by about £120 million in 1983-84. Each 10p off CB is worth about £20m.

7. If oil prices fell after the Budget then the arguments put forward in my submission of 11 February would apply. Briefly, if early fiscal action were required it would probably have to take the form of higher indirect taxes. The present regulator powers seem fully adequate to produce revenues on the scale needed - these allow excise duties to be varied, selectively or across the board, by up to 10 per cent and the VAT rate to be changed by up to 3¾ points in either direction. Fully used from the beginning of the financial year, the excise duty regulator could raise about £1 billion of revenue in 1983-84 and the VAT regulator about £2½ billion. On a longer view, it would be desirable, assuming the lower oil price looked likely to be "permanent", to make good part of the PSBR loss by reducing public expenditure. Sir Anthony Rawlinson is putting in a separate submission

on this. It is difficult to see much being achieved by this route in the short-term.

8. We can elaborate on some of these options in more detail next week.. But I hope this note gives some idea of the possible size of the problem and of the kind of options available.

F CASSELL

b/f 9/3.

From: T Burns
4 March 1983

CHANCELLOR

Ta for very thorough analysis — which is hardly convincing. Does CST/EST have any views?

G.H.

FR Pl. note.

Note
Asked for CST + EST's views
7/3

cc: Chief Secretary
Economic Secretary
Sir D Wass
Mr Middleton
Mr Cassel
Mr Evans
Mr Kemp
Mr Odling Smee
Mrs Lomax
Mr Bell
Mr Ridley
Mr Harris

THE CASE FOR A BALANCED BUDGET

1. The Times leader of 10 February advocated a balanced Budget. The case is based on two arguments. Significant deficits (defined as anything above 5 per cent of national income) are always inflationary. A small deficit may be acceptable on economic grounds, but political considerations point to a balanced Budget - it is simple, catches the eye and makes the connection between expenditure and taxation abundantly clear.

2. The leader argues that "the PSBR is not the appropriate deficit concept for the Government to watch" because it includes the Nationalised Industries. Like other commercial organisations, the NIs should be allowed to borrow to finance their investment programmes. It is borrowing that arises out of the activities of central and local government and should be balanced, not the PSBR.

3. Sam Brittan criticised this line of argument in the Lombard column, though he endorsed the Times' point about NIs investment (and extended it to cover all public sector capital expenditure). More generally he posed this question to a would-be Budget balancer: "Which of the dozens of possible balances would you like to see at zero?" The alternatives are arrived at by combining adjustments for inflation (the so-called "real" PSBR), the cycle, public capital expenditure or National Industries. Adjusting for any one of these (except the last) would give a Budget surplus according to Mr Brittan. This means that the

/ UK's

UK' public sector finances, far from being in deficit, are showing a substantial surplus.

4. Sam Brittan's general guiding principle is similar to that of the Times, though he does recognise the need to provide for economic growth - policy should be set "to provide a stable upward path of national income and expenditure to sustain non-inflationary growth". But he sees "policy" as both monetary and fiscal. The mix determines interest rates. If private sector investment is too low, this signals that fiscal policy is too lax - whatever the number for the deficit might be.

Comment

5. A balanced Budget would undoubtedly have some presentational attractions. It would be one way of demonstrating a commitment to stable prices. It would also make the relationship between taxation and expenditure more transparent. In practice, of course, we would probably want to allow for year-to-year variations, to take account of cyclical fluctuations in the economy - as we do now. But if surpluses and deficits cancelled out over a run of years, borrowing could not be regarded as an easy alternative to increases in taxes or cuts in spending.

6. But there are considerable difficulties in applying this proposal to the current definition of the PSBR:

(i) the PSBR is a rag bag of items, more associated with accounting conventions than economic analysis. An objective of reducing the PSBR to zero would look like a very precise target. This would highlight some tricky definitional issues which, for want of a better solution, we have managed to sidestep in recent years by arguing that the PSBR is not a target in its own right;

(ii) from an economic point of view, it is not clear that fiscal policies, consistent with zero inflation, would involve a zero PSBR. Even with zero inflation, economic growth would probably generate some trend increase in the demand for financial assets, including public sector debt and money.

/ 8.

8. The case for positive public sector borrowing rests, to some extent, on the fact that the public sector does a substantial amount of investment. Borrowing to finance profitable investment yields an income to set against future interest payments. Both the Times and Sam Brittan are arguing, in effect, that the appropriate definition of the budget to balance is one which excludes some, or all of public sector investment. The strength of this position depends critically on whether it is, in fact, appropriate to draw a strong distinction between investment and other sorts of public spending. We have been very sceptical about this, eg. in evidence to the Select Committee.

9. The first part of this note looks at the arguments for a balanced budget in the context of the present definition of the PSBR. The second part considers whether it would be helpful to point to some alternative definition of the budget balance, for which zero might be an appropriate long term objective.

I. The Consequences of a Zero PSBR

10. In previous versions of the MTFS we have placed some weight upon the argument that the PSBR must be fixed at a level which will match the private sector's demand to hold public sector debt at acceptable interest rates. The argument is that there is an underlying demand for financial assets including public sector debt and money. A fiscal deficit and monetary growth just sufficient to satisfy this demand should not raise interest rates, nor should they be inflationary. Just as the rate of monetary growth consistent with zero inflation would almost certainly be positive, so a consistent fiscal stance is likely to involve a small borrowing requirement.

National Debt and Income

11. It is difficult to quantify these propositions with any precision. Chart 1 shows the historic relationship between the PSBR and GDP; Charts 2 and 3 show how ratio of public sector debt to income has changed over the past. The broad pattern is of sharp rises in the debt ratio during war time, which are then very gradually reversed. Since the Second World War, public sector debt has grown about 2-4 per cent a year more slowly than money incomes, though the downward trend has been much less pronounced since the mid 1970's.

/ 12.

12. In the latest NIESR Review, Andrew Britton argued that the fall in the debt income ratio in the early '70s was, in part, a response to unanticipated inflation. He therefore suggested that the private sector might be willing to increase the amount of debt it holds much more rapidly, in the immediate future, without unacceptable consequences for interest rates. A more cautious view might allow for a growth in the private sector's demand for debt broadly in line with income. On this basis, a PSBR of about 1 per cent might be consistent with stable prices, and an underlying growth in the economy of around 2 per cent or so. A lower figure - closer to balance - could be justified, if one took the view that the downward trend observable over the whole post-war period was likely to resume.

Would a balanced Budget be deflationary?

13. It is difficult to say with any confidence what PSBR is likely to be consistent with zero inflation. What are the consequences of getting it wrong? The effects of excessively high deficits are familiar enough. A PSBR that is too high in relation to the monetary targets is likely to require high and rising interest rates, which would put upward pressure on the exchange rate, and squeeze private investment. These arguments apply in reverse. An excessively tight fiscal stance, relative to money supply, implies continuous downward pressure on interest rates, and possibly the exchange rate.

14. The risk is that a low PSBR would be excessively deflationary. In part, that depends on how far lower interest rates and a lower exchange rate can be relied upon to stimulate private sector investment and output. In the past few years, high interest rates have probably had a greater effect on activity than previously estimated, and this might provide grounds for optimism about the expansionary effect of very low interest rates, at least in current circumstances.

15. In the context of low or zero rates of inflation, however, the risks of an excessively tight fiscal stance may be greater. There is a floor to nominal interest rates - zero is the absolute minimum (because you can earn this just by holding cash) and, historically, long rates have never fallen below 2 per cent, even whenprices were

/ falling.

fa' ing. Once this floor has been reached, a tight fiscal policy will depress activity and ultimately prices. This would raise real interest rates and further deflate the economy. This is Keynes' famous liquidity trap. It is often forgotten that real interest rates were very high between the wars - typically above 5 per cent - precisely because prices were falling.

16. To sum up, stable prices probably point to a small fiscal deficit, rather than a zero PSBR. Indeed, if a balanced budget (on this definition) led to a fiscal squeeze that actually forced down prices, private investment and activity could be severely depressed.

II. Redefining the Budget Balance

17. It is often argued that the Government should judge the scale of its borrowing in relation to the size of its investment programme. Neither the Times nor the Financial Times want to restrict borrowing to finance at least some kinds of public investment. That is why they propose a narrower definition than the PSBR as the basis for a "balanced budget".

18. In principle there undoubtedly is an important difference between current and capital expenditure. Borrowing to finance investment leaves an asset to match the liability, which would yield an income to set against future interest payments. Current expenditure does not generate a direct return to pay for the borrowing to finance it. It follows that, if the NIs behaved just like private firms, it would be odd for the Government to closely control or seek to minimise the borrowing of one but not the other. A profitable investment financed by borrowing should generate the returns sufficient to repay the loan with some additional pure profit.

19. Of course the initial loan would still place demand on the capital market, and tend to raise interest rates and crowd out other investments. But this is an essential part of the market mechanism by which entrepreneurs bid for scarce funds. If the public sector projects are profitable they should have access to those funds. In this way the discipline of the market place ensures that the total return for the nation's investment is maximised.

/ 20.

20. One way to avoid distorting Nationalised Industry activities would be to remove their borrowing from the control total, as suggested by the Times Leader, by focussing upon the General Government own account borrowing requirement. This takes out the Nationalised Industry total borrowing requirement (including loans to NIs from Central Government).

21. Table 1 shows the magnitudes over the past few years and a comparison with the historical average. Historically the difference between the PSBR and the General Government own account borrowing has averaged around $1\frac{3}{4}$ per cent of GDP. In recent years it has been lower.

indeed negative

22. The problem with this approach is that the rate of return on Nationalised Industry investment has been very low.* This may reflect a number of considerations: government price restraint; social considerations; adjustment problems of large declining industries. But as Nationalised Industries investment has generally yielded a return below the real cost of borrowing it must be included in the control total for borrowing if it is to be financed in a non-inflationary way. In other words, a net subsidy to NIs has to be financed by higher taxes and/or lower expenditure elsewhere.

23. In principle, one way round this problem would be to assign a lower weight to public investment than to current spending in calculating the PSBR, with the weights depending on the commercial viability of the investment concerned. This might be done by "annuitising" (ie. converting the capital sum into income stream) Nationalised Industries' investment at its rate of return less the average market rate. If the two rates of return were the same this would amount to excluding NIs. If the return on NI investment was zero, this would imply treating it on all fours with current spending. Obviously, even if this principle was correct, the practice is unlikely to be straightforward.

and would be ridiculed

24. Other ways of redefining the PSBR raise similar issues. For example, some would argue that some elements of general government investment should be financed by borrowing (and excluded from the

/ control

* See Chart 5

control total) since they yield a long term rate of return, even if that cannot be readily measured in financial terms. By an extension of the same reasoning, there could be a case for focusing only on the general government's current surplus or deficit. Whatever the intuitive appeal of these proposals, they open up a very difficult area: the measurement of rates of return on public service investment; the choice between those expenditures classified as capital and current spending; indeed the wide variety of issues that eventually persuaded the Treasury to abandon the distinction between above and below the line.

Presentational Aspects

25. It is possible to look at other definitions (there is no shortage - see table 1). But it would not be simple, and redefinition might itself defeat the major presentational advantage that announcing a balanced budget objective would bring. It might also reopen the argument for redefining the PSBR itself.

Conclusion

26. My conclusions are as follows:

(i) There are a number of reasons why it would be wrong to aim for a zero PSBR (as currently defined) even if zero inflation was the objective.

(ii) There are a number of difficulties in excluding nationalised industries' investment from the budget deficit; particularly the problem of the low rate of return on their investment.

(iii) It is even more difficult to find a consistent treatment for other forms of public sector investment. It really is very difficult to "draw the line".

27. One way forward is to remind people of the reasons why "sound finance" does not necessarily mean a zero PSBR. You can hint at the role of public sector investment in determining the extent of borrowing without being committed to it as the sole reason. Given the uncertainties discussed here, however, it is important not to make any

/ precise

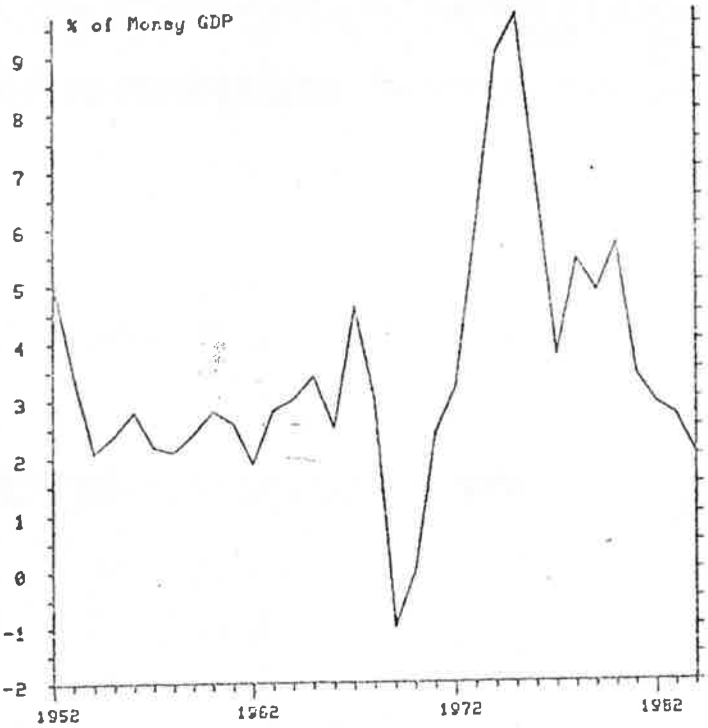
pr(.se statement about the appropriate size of the PSBR that is consistent with a balanced budget on any particular definition.

28. You may like to discuss this with us. We can, in time, produce a more extensive analysis if you wish but I suspect this is a blind alley. The main conclusion that is relevant to thinking about your Budget Speech, argues against taking up any committed position on balanced budgets whilst continuing to aim for a PSBR path that we judge to be appropriate for the inflation objective.

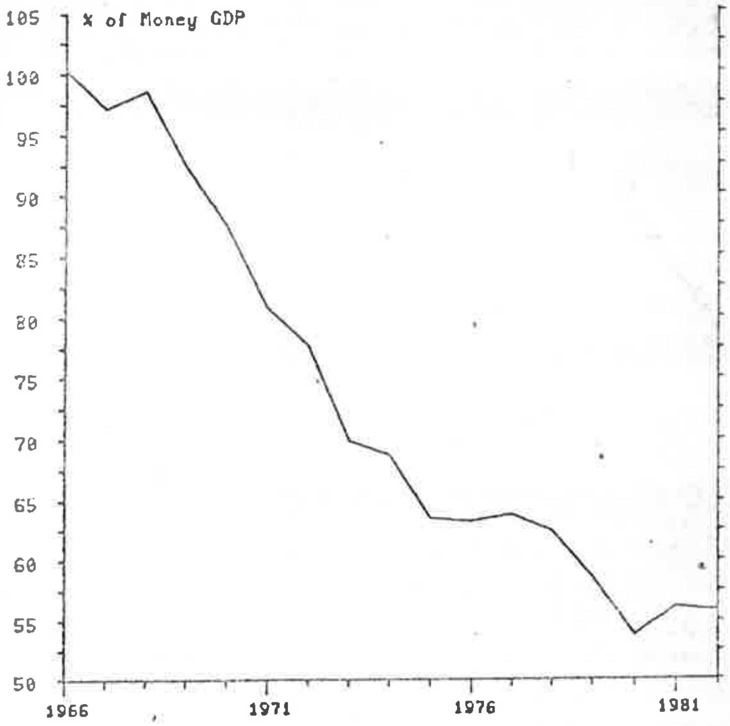
TB

T BURNS

1. PSBR 1952-1982

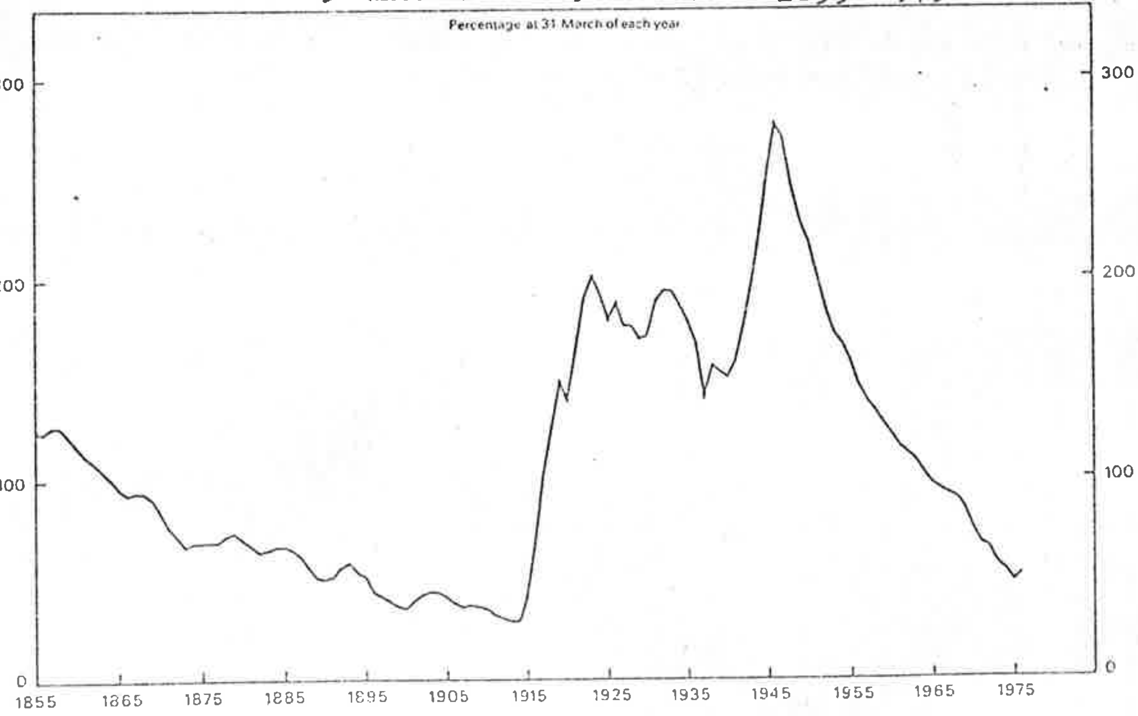


2. Total Public Sector Debt 1966-1982



3. Ratio of national debt to gross national product 1855-1975

CHART 3



4. Public Sector and General Govt Borrowing Reqt.

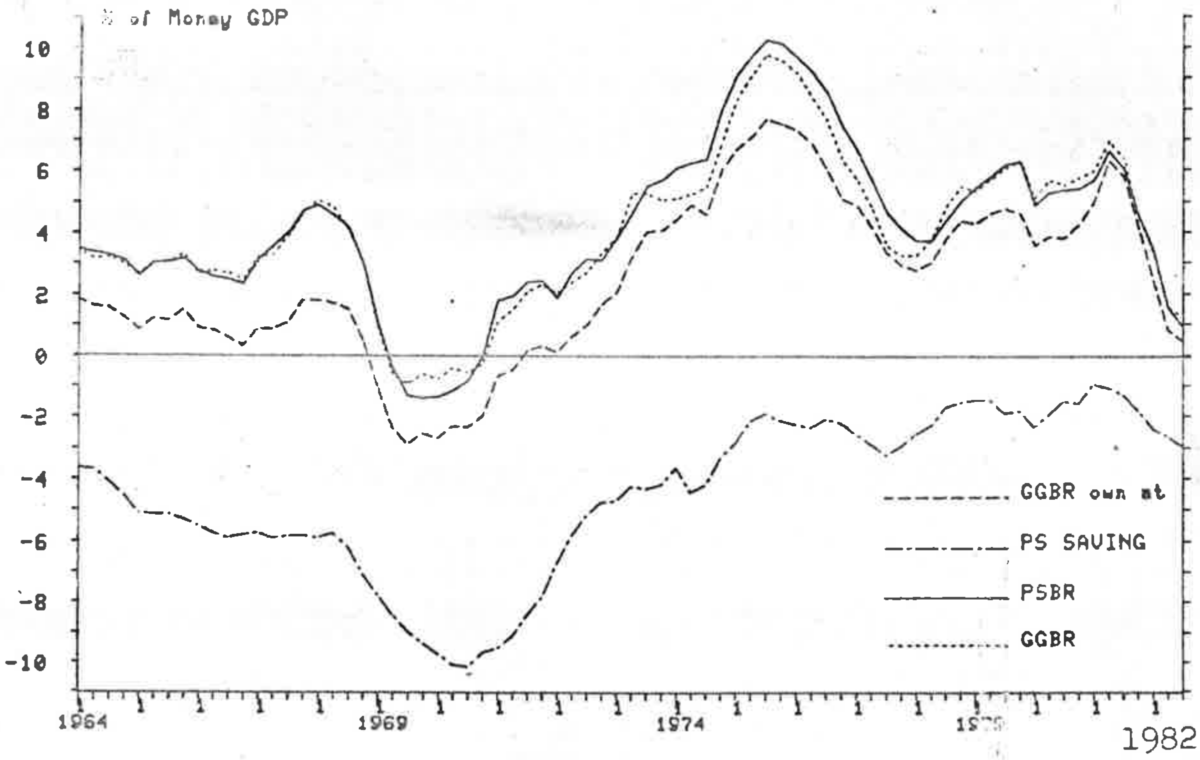


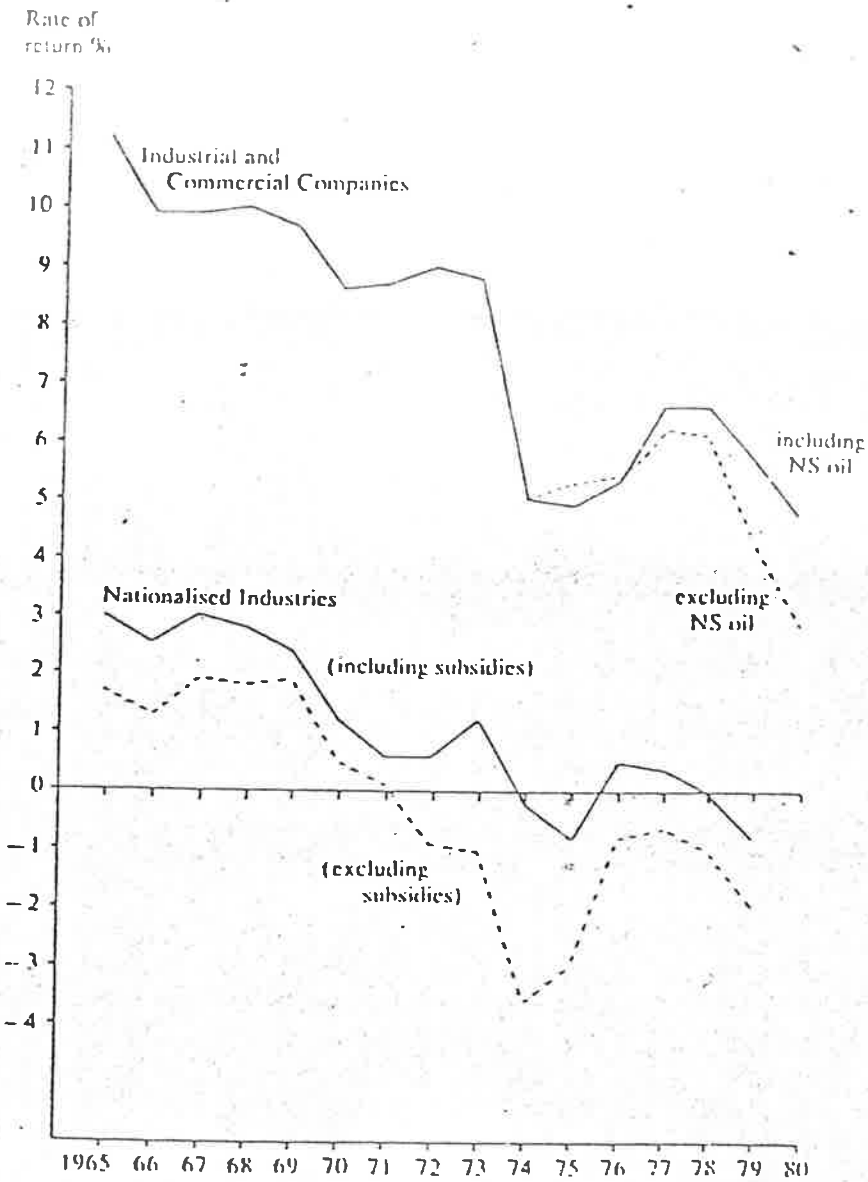
Table 1 : Alternative Budget Measures

% of Money GDP	General Government: Borr. reqt.	Own Account Borrowing	Current Savings*	Public Sector: PSBR	PSBR less Pub. Corps Investment	PSBR less pub. sector investment	PS Current Savings*
1979-80	5.1	3.6	-0.4	4.9	2.0	-0.7	-2.5
1980-81	6.0	5.0	0.9	5.7	2.7	0.3	-1.0
1981-82	3.4	2.4	-0.3	3.5	0.6	-1.1	-2.4
1982-83 (January Forecast)	3.3	2.4	0.0	2.9	0.1	-1.[illegible]	-2.3
Averages							
1963-64 to 1970-71	2.3	0.2	-4.8	2.3	-1.3	-5.9	-6.6
1970-71 to 1981-82	4.8	3.6	-1.6	5.2	2.0	-1.8	-3.5
1963-64 to 1981-82	4.0	2.4	-2.6	4.1	0.8	-3.3	-4.5

* Net savings are shown as negative to correspond with the sign convention for the PSBR

CHART 5.

PRE-TAX REAL RATES OF RETURN ON CAPITAL EMPLOYED*



*Defined as gross trading surpluses plus rent received, less capital consumption at replacement cost and less stock appreciation, as a percentage of net capital stock at replacement cost plus the book value of stocks.

SOURCE: Treasury Memorandum to TCSC,
Report on Financing of Nationalised Industries
HC 348(II) - July 1981

10 FEB 1983

TIMES

A BALANCED BUDGET

Price stability should be the Government's central economic objective and monetary policy should be the main instrument to achieve it. But what then is the role of fiscal policy?

In principle the dominant approach for most of the post-War period was Keynesian, with the budget deficit being varied to correct departures from full employment. The idea was that if unemployment became too high, government spending would be raised and the budget deficit increased in order to promote demand. In practice fiscal policy had to be far more cautious throughout the 1950s and 1960s because of the need to maintain a satisfactory balance-of-payments position and so protect the sterling exchange rate. Very large budget deficits began to be recorded only after the end of fixed exchange rates in 1972.

The most extravagant year was 1975/76 when the public sector borrowing requirement approached 10 per cent of gross domestic product. Since then there has been a striking change. This year the PSBR should be about $2^1/_2$ per cent of gross domestic product. As most other countries have simultaneously expanded their budget deficits, Britain now has the lowest ratio of government borrowing to national income in the OECD area.

The universal trend towards highter budget deficits has not had the effects that the Keynesian textbooks predicted. Far from leading to a decline in the numbers out of work, it has coincided with big increases in unemployment throughout the industrialized world. The Keynesian argument has been contradicted most recently in the United States, where a record budget deficit is now being blamed for less output and higher unemployment when in theory it should have caused more output and less unemployment.

Unhappy experience over the last decade justifies scepticism about the appropriateness of using fiscal policy to regulate employment and, indeed, about the desirability of placing undue emphasis on full employment as a government responsibility. The right question, then, is not "what short-run change in the budget deficit is needed to improve employment in any particular year?", but rather "what fiscal rule is consistent with the maintenance of price stability in the long run?"

One way of tackling this question is to consider what type of fiscal policy is clearly inconsistent with price stability. It is obvious that substantial and continuous budget deficits, amounting to 5 per cent or more of national income, are difficult to reconcile with sound monetary policy. The deficits cannot be met to an unlimited extent by long-term savings from the general public and financial institutions, but must sooner or later be covered by short-term borrowing from the banks. Such borrowing increases the money supply and tends to be inflationary.

By contrast, if the budget is balanced, fiscal policy poses no serious threat to the pursuit of non - inflationary monetary policy. Since the government has no need to borrow at all, it does not have to borrow from the banks or print money. There may still be excessive monetary growth because of too much bank credit to the private sector, but that can be reined back by raising interest rates and does not require special action on government spending or taxation. A balanced budget is clearly consistent with, although not necessarily sufficient for, price stability.

This does not establish a conclusive case for a balanced budget. There is a grey area with moderate budget deficits of less than 5 per cent of national income which it may be possible to finance for many years in a non-inflationary way. The objections to small budget deficits are probably as much political as economic. Two are particularly important.

First, the notion of a balanced budget is easy to understand. In an age when economic policy has become complicated to present and explain, there is obvious merit in adopting a fiscal rule which everyone can respect because of the transparency of its intentions. A major drawback of the medium-term financial strategy was that fiscal goals were stated in terms of "the PSBR as percentage of g.d.p.". As this phrase is meaningless to most people, the announcement of the strategy did not have the favourable impact on expections that was originally hoped.

Secondly, the commitment to a balanced budget highlights the connexion between expenditure and revenue. This may seem a trite and superfluous observation, but there is little doubt that until quite recently the structure of fiscal decision-taking encouraged every minister to put up inflated bids for his own department's spending in Cabinet meetings. Since the size of the budget deficit was determined by the level of demand in the economy and decided by a process quite separate from that which fixed total public expenditure, no individual minister had to worry about the strain his department's spending would impose on the nation's resources.

If a balanced budget rule were adopted, several technical issues of definition and implementation would have to be resolved. It should be said straightaway that the PSBR is not the appropriate deficit concept for the Government to watch. The PSBR is affected by the operations of nationalized industries. As they resemble commercial companies in having investment programmes which are financed by continuous borrowing, it would be wrong to prevent them borrowing because of a balanced budget rule. More sensible than the PSBR as a target would be the net financial position of central and local government combined. Also contentious is the question of whether the government's finances should be balanced every year or over the course of the business cycle. A requirement to balance the books over the cycle would be less rigorous since it would contemplate deficits in recession years.

After so many years of deficits and borrowing, it may seem unrealistic or even utopian to propose a balanced budget as a reinforcement of non-inflationary monetary policy. But balanced budgets were the norm in Britain before the Second World War and until then the price level showed no tendency to increase over very long periods. Even the 1944 *Employment Policy* White Paper, supposedly a charter for Keynesian demand management of the most permissive kind, stated that " an undue growth of national indebtedness will have a quick result on confidence", and therefore the "need for a policy of budgetary equilibrium such as will maintain the confidence in the future which is necessary for a healthy and enterprising industry". Those words are as pertinent today as when they were written.

Lombard

Futile quest for balanced budget

By Samuel Brittan

IT LOOKS as if the British Government is well ahead of schedule in its plan for a phased reduction of the Public Sector Borrowing Requirement (PSBR). According to some guesses it will be down to about £7bn or 2½ per cent of the Gross Domestic Product in the financial year 1082-83.

Why not, it is tempting to ask, complete the process as soon as possible and go for a "balanced budget?"

Unfortunately this attractive-sounding notion is a mirage. In Gladstone's time, when there was little public capital expenditure and no embedded inflation for which to adjust, a "balanced budget" had some meaning. But today, one would have to ask a budget-balancer: "Which of the many dozens of possible balances would you like to see at zero?"

These are not petty quibbles over small magnitudes. Let us suppose that we allow for the state of the business cycle and accept deficits in years of recession in the hope of recouping them in time of boom? The size of the cyclical adjustment is very sensitive to judgements about what is a "normal" rate of activity and employment. The Simons and Coates adjustment, which is far more modest than some, as it takes as base the year 1979 when unemployment was nearly 1¼m, shows that on a cyclically-adjusted basis there was no deficit, but an overall surplus repayment of more than £4½bn.

Another adjustment, involving less "theory," is for inflation. When prices rise the real value of government debt falls. This is similar to the "gearing" adjustment advocated for company accounts. The adjustment increases the overall public surplus to about £12bn.

But that is not the end of the matter. The most respectable people argue that public capital expenditure, designed to improve the physical and social "infrastructure," can be legitimately financed from borrowing. Taking the three adjustments together, the current budget surplus works out at £26bn to £30bn or 10 per cent of GNP. Any one of the adjustments alone would be enough to turn the PSBR into surplus.

Thus pressing for a "balanced budget," so far from helping the "sound money" cause, will merely bring forth a spate of learned calculations to show how violently the Government has overbalanced its accounts. When officials reply, the discussion will get diverted into a futile scholastic argument about whether the budget is "really" in surplus or deficit. The much more important, but admittedly difficult, question is whether the combined stance of fiscal and monetary policy—by whatever measure we choose to use—is likely to provide a stable upward path of national income and expenditure to sustain non-inflationary growth.

If non-inflationary growth of monetary demand were found to involve serious budget deficits over the very long term, it would be a *prima facie* sign that excess savings were being used for consumption, and it would be sensible to change the policy mix towards lower interest rates, in the hope of promoting investment.

But even if one is sceptical of the cyclical and inflation adjustments and doubtful about how much of the £15bn of public investment is producing a return, it is extremely difficult to argue that public savings are anything but positive. Thus the problem of structural deficits does not arise in Britain at the present time, in sharp contrast to the U.S.

ALTERNATIVE MEASURES OF BUDGET BALANCE

1982-83

	£bn	% of GDP
Public Sector Borrowing Requirement	− 7.2	− 2.6
General Government	− 7.5	− 2.7
General Government, cyclically adjusted	+ 4.7	+ 1.7
General Government, cyclically and inflation adjusted	+12.2	+4.5
As above, deducting capital expenditures	+27.2	+10.0

CONFIDENTIAL

cc. Chancellor
Financial Secretary
Economic Secretary
Minister of State (C)
Minister of State (R)
Sir Douglas Wass
Mr Middleton
Mr Kemp
Mr Moore
Mr Robson
Mr Griffiths   Mr Martin

CHIEF SECRETARY TO THE TREASURY

Treasury Chambers, Parliament Street, SW1P 3AG

Mr Salveson
PS/IR
Mr P Lewis I/R
PS/C&E
Mr Howard C&E

Mr P Graham
(Parly Counsel)

Murdo Maclean Esq
Private Secretary
Chief Whip
12 Downing Street
London SW1

4 March 1983

DWP

Dear Murdo

FINANCE BILL: AMENDMENT OF THE LAW RESOLUTION

I attach a minute that the Chief Secretary has received on the form of the Amendment of the Law Resolution for the Finance Bill and on whether we are to have the usual Incidental Charges Resolution. You will see that it recommends that we should table the standard ALR used in recent years. You will recall that last year the Chief Whip was consulted on this question - mainly because the standard ALR would preclude amendments or debate on VAT relief for charities. The Chief Secretary would be inclined to use the standard Resolution again this year but before making a final decision he would be grateful for confirmation that the Chief Whip would be content with this.

Yours sincerely

JSG. Gieve

JOHN GIEVE
Private Secretary

CONFIDENTIAL

CH/EX REF NO B83\6

COPY NO 9 OF 10 COPIES

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

PRIME MINISTER

THE BUDGET

In this minute I set out the Budget plans, which remain along the lines we have previously discussed. I envisage no major changes - except in the event of a very substantial further fall in the oil price in the next few days.

2. I plan to hold to the figuresfor monetary growth set out in the 1982 Medium Term Financial Strategy - ie ranges of 7-11 per cent for next year, 6-10 per cent for 1984-85 and 5-9 per cent for 1985-86. As before these paths apply to both the narrow and broad measures of money. I hope that we shall hit the middle of the ranges. I have given a good deal of thought to the possibility of reducing at least the top of these ranges by one point. But there is some disadvantage in revising medium term objectives in two successive years. And it is clear that the announcement of a downward move could make it significantly more difficult for us to go on getting interest rates down. In present circumstances, I regard that as decisive.

3. At the time of the last Budget, and again last Autumn, I proposed a figure for the 1983-84 PSBR of 2¾ per cent of GDP, and I plan to hold to this too. For this year (1982-83) we shall publish a forecast out-turn figure of some 3 per cent. The 1984-85 figure, after taking account of the Budget measures and allowing for a future "fiscal adjustment" of £0.5 billion, is forecast at 2½ per cent. Although the nominal figures will coincidentally be £8 billion in all three years, we shall thus continue to show a downward trend as a percentage of GDP.

4. On the basis of the present forecast, an £8 billion PSBR next year gives scope for tax reductions with a PSBR cost of some £1½ billion,

over and above revalorisation of thresholds and excise duties. This figure, however, understates the total reductions we shall have effected for the year 1983-84 because it does not take account of the measures I announced in the Autumn. I shall, of course, ensure (with due discretion) that these are not overlooked.

5. The Annexes below provide a summary of the detailed proposals. Where they have a public expenditure cost it will be accommodated within the Contingency Reserve, and will not lead to any increase in plan totals.

6. As you see, the lion's share of the initial benefit goes to individuals rather than to industry. We both think this is right, given the need to tackle the poverty and unemployment traps, and the way we have favoured industry in previous years, (eg by not increasing thresholds in 1981). Industry is, of course, the main beneficiary of the measures which we announced in the Autumn - and is also helped by the lower exchange rate.

7. The main line of attack on our plans will I think be that we are proposing a "Budget for the Better Off". As you know, I plan to raise all the income tax thresholds and allowances by 8½ per cent over indexation. Using the Government Actuary's earnings assumption of 6½ per cent, this will reduce or match average rates of tax and NIC for 1982-83 for all those contracted-in. But the perceived effect of course is to confer the greatest benefit on the better off and critics will seize on the point that the immediate effect of the Budget changes will be that at fixed levels of income (the so-called static comparison) taking the changes in tax with the NIC increases, married men on salaries of less than £16,000 a year will gain only up to £100 in 1983-84 (and some single people or a few on contracted-out schemes will actually lose.) Yet a married man on £30,000 a year will gain some £600.

8. The increase in the mortgage interest relief ceiling will also give most benefit to the better off. And no doubt our critics will add our plans for social security upratings to their indictment.

9. But there is no sensible way of preventing the perceived effect of increases in the income tax thresholds. One could in theory increase the higher rate bands less than the basic rate thresholds - or even freeze them, as happened over many years in our political youth. But that allows inflation to make the rate structure even more steeply progressive than it already is, and would be wholly wrong. Even if we were to do no more than index the higher rate bands, our £30,000 a year married man would still gain by about £450, and we should scarcely have blunted our opponents' attack. The truth is that all the thresholds and bands suffered similarly from the absence of indexation in 1981; and that all should be corrected now if we are to restore the rate structure - though not yet the levels - set in my 1979 Budget.

10. All this increases the political importance of a number of - not very costly - other measures, viz the increase in child benefit to £6.50, which is above the April 1979 level; the unemployment package we have discussed, together with action on unemployment benefit; extension of the widow's bereavement allowance; removal of the invalidity trap, and so on - the full list is in table 2 of Annex B below. Another useful counter-weight to criticism is the group of minor measures against corporate tax avoidance and fringe benefits listed in table 6 at Annex B.

11. On the positive side, for business and enterprise I am proposing packages of measures to help small and new businesses - including a major simplification and extension of the Business Start-up Scheme, now extended to all existing unquoted companies; new technology - including a £100 million re-introduction of the SEFIS scheme; the construction industry; and wider share ownership. This is all in addition to the further ½ per cent cut in NIS which we discussed some weeks ago: I am sure that it is politically necessary to cope with the "pure" industrial lobby, which has significant backbench support, not least in the West Midlands.

... 12. I attach at Annex A a summary of the costs of the main proposals. Annex B lists the minor items. You may also wish to glance at the commentary by officials at Annex C.

13. I am sending you a separate note on the oil taxation proposals which I have agreed with Nigel Lawson.

(G.H.)
4 March 1983

£ million

	1983-84 PSBR	1983-84 REVENUE	1984-85 PSBR	1984-85 REVENUE
Individuals				
Personal Allowances	1010	1170	1060	1490
Housing and Home Ownership (Table B1)	80	115	65	105
Social Security (Table B2)	75	125	190	320
Unemployment (Table B3)	25	55	40	75
	1190	1465	1355	1990
Businesses and Industry				
Corporation Tax	35	40	60	70
National Insurance Surcharge	200	220	300	400
Small Firms and Enterprise (Table B4)	25	35	130	165
Technology and Innovation (Table B5)	30	40	50	80
	290	335	540	715
North Sea Oil	105	120	85	100
Specific Duties	(10)	(10)	(10)	(10)
Miscellaneous (Table B6)	-	-	(30)	(45)
GRAND TOTAL	1575	1910	1940	2750

Note 1: The measures include both tax and public expenditure elements. For tax the costs shown are the excess over indexation; for public expenditure the excess over what is already provided in the PEWP.

2: The figures shown are rounded and may still vary marginally. The specific PSBR costs shown for each group of measures is necessarily approximate.

ANNEX B

TABLE 1

HOUSING AND HOME OWNERSHIP

£ million

		1983-84	1984-85	Full Year
1.	Enveloping*	50	nil	-
2.	Mortgage Interest Relief ceiling - increase to £30,000	50	85	60
3.	Improvement grants*	10	10	-
4.	Stock relief: householders part exchange simple scheme	under 1	5	5
5.	Self-employed second home mortgage interest relief	2	5	5
	Revenue costs	52	95	70
	Public expenditure costs	60	10	-
	GRAND TOTAL	112	105	70
	Taken as	115	105	

Note: Items marked * are public expenditure

ANNEX B
TABLE 2

SOCIAL SECURITY

£ million

		1983-84	1984-85
1.	Abolition of £25,000 limit for CTT exemption on gifts to Charities	under 1	under 1
2.	Deeds of Covenant - increase in ceiling for higher rate		3
3.	Tax relief for staff seconded by companies to voluntary bodies	under 1	under 1
4.	Extension of widow's bereavement allowance	25	30
5.	Raise cut-off for SB resources to £3,000 *	2	7
6.	Raise cut-off for SB single payments to £500 *	1	3
7.	Real increase in therapeutic earnings limit *		
8.	New mobility supplement for War Pensioners *		
	Less housing benefit savings	(2)	(6)
9.	Restoration of 5 per cent abatement in UB *	22	59
10.	Increase child benefit to £6.50 per week, plus corresponding rise in one parent benefit *	74	212
11.	Removal of invalidity trap *	4	14
	Revenue costs	25	34
	Public expenditure costs	101	290
	GRAND TOTAL	126	324
	Taken as	125	320

* Public expenditure items. Costs are those over and above amounts provided for in the White Paper

ANNEX B

TABLE 3

UNEMPLOYMENT

£ million

	1983-84	1984-85
DHSS early retirement (automatic credits 2, long-term SB 22)*	24	24
Enterprise allowance: cash limited nationwide scheme, plus spill over (gross)*	25	25
Part-time JRS from 62*	5	25 ≠
GRAND TOTAL	54	74
Taken as	55	75

Note: Items marked * are public expenditure

≠ £25 million is provisional estimate

SMALL FIRMS, ENTERPRISE AND WIDER SHARE OWNERSHIP

£ million

		1983-84	1984-85	Full Year
1.	Business Expansion Scheme	nil	75	75
2.	Loan Guarantee Scheme*	nil	nil	-
3.	Wider share ownership	20	30	40
4.	Capital Gains Tax (see note 1)			
	a. monetary limits	nil	1	1
	b. retirement relief	nil	1	4
5.	VAT registration thresholds	5	10	10
6.	De minimis limit for assessment of apportioned income	under 1	under 1	under 1
7.	Acceptance credits	1	1	1
8.	Capital Transfer Tax (see note 2)	8	18	20
9.	Zero/deep-discounted stock	neg	15	15
10.	Relief for interest, employee buy-outs	1	1	2
11.	Tax treatment of interest paid by companies to non-residents	under 1	under 1	10
12.	Increase in proportion of office space qualifying for industrial building allowance	nil	10	25
13.	DLT - extension of own-use deferment	nil	under 1	4
14.	Small Workshop Scheme - averaging for converted premises	under 1	under 1	under 1
	GRAND TOTAL	36	163	208
	Taken as	35	165	

Note: Items marked * are public expenditure

1. The cost of these CGT measures when statutory indexation is added is nil, 5 and 15 million.

2. Indexation of CTT costs 15, 30 and 45 respectively. The additional costs shown for item 8 are for rounding up the indexed thresholds, for extending the instalment period from 8 to 10 years, and for increasing reliefs on let land and unquoted companies to 30 per cent.

TECHNOLOGY AND INNOVATION

£ million

		1983-84	1984-85	1985-86
1.	Extension of transitional period for capital allowances - films	nil	nil	30
2.	Extension of transitional period for capital allowances - teletext TVs	nil	10	15
3.	SEFIS*	20	40	40
4.	Information technology*	5	8	11
5.	Innovation linked investment*	5	15	20
6.	Advisory services*	9	6	6
7.	Science Parks* (included above)			
	Revenue costs	nil	10	45
	Public expenditure costs	39	69	77
	GRAND TOTAL	39	79	122
	Taken as	40	80	

Note: Items marked * are public expenditure

The cost of the whole package over three years is £240 million

ANNEX B
TABLE 6

MISCELLANEOUS

£ million (yields)

		1983-84	1984-85	Full Year
1.	Car and car fuel scales - 15 per cent average increase	nil	(25)	(30)
2.	Cheap housing for directors	nil	nil	(1)
3.	Life assurance: chargeable events: secondhand bonds	under (1)	under (1)	under (1)
4.	CGT: non-resident trusts	under (1)	under (1)	under (1)
5.	CTT: remove special deemed domicile rule for Isle of Man etc	1	2	2
6.	Group relief: avoidance (BL)	nil	(10)	(10)
7.	DLT: disposals by non-residents	(1)	(2)	(2)
8.	Taxation of international business. Offset by Double Taxation Relief against Corporation Tax	nil	nil	nil
9.	Beneficial mortgage loans from employers	nil	under (1)	under (1)
10.	Directors PAYE tax	nil	(10)	(10)
11.	TSBs to be treated as bodies corporate	3	10	10
	GRAND TOTAL	2	(47)	(52)
	Taken as	-	(45)	

Annex C.

INDIVIDUAL MEASURES

Personal Allowances

1. All thresholds and allowances (including the higher rate and IS thresholds) to increase by 14 per cent, or 8½ per cent above the statutory minimum. This will for the great majority of people (but not quite all) more than outweigh the increased National Insurance Contributions which come into effect in April.

Social Security etc.

2. Child benefit to increase to £6.50 per week, taking its value above the level inherited in 1979. There will be a parallel increase in one-parent benefit. The 5 per cent abatement in unemployment benefit, effected in 1980, to be restored; widows bereavement allowance to be extended to a second year; the invalidity trap to be eliminated. Should go some way to offset the criticism on general social security upratings.

Housing and Home Ownership

3. This group includes the increase in the Mortgage Interest Relief ceiling from £25,000 to £30,000. Also included are proposals to provide more for Home Improvement Grants, and also to provide money for so-called "enveloping" schemes, under which local authorities repair the external fabrics of complete streets or terraces, as part of helping counter the problems of housing decay.

Unemployment

4. The measures here include proposals in respect of early retirement, a nationwide extension of the Enterprise Allowance Scheme, and making the Job Release Scheme available to part-timers from the age of 62.

Corporation Tax

5. Reduce the small companies rate from 40 per cent to 38 per cent, and alter the limits so as to reduce the transitional marginal rate.

National Insurance Surcharge

6. Cut NIS by ½ per cent for the private sector only, from next August. Complete abolition of the Surcharge is the single measure most frequently and forcefully pressed in industrial representations.

Small Firms, Enterprise and Wider Share Ownership

7. A major extension and simplification of the Business Start-Up Scheme, to be called the Business Expansion Scheme. The principal change is the extension of the present scheme to provide tax relief for equity investment not just in new companies but in all qualifying established unquoted trading companies. (Following a review, other changes are being made to make the scheme less restrictive.) Also further measures to encourage wider share ownership, improvements in the Capital Transfer Tax regime, an extension of the Loan Guarantee Scheme, and an increase in the VAT registration threshold.

Technology and Innovation

8. The major measure is the re-opening, at a cost of £100 million over the next three years, of the Small Engineering Firms Investment Scheme (SEFIS). Also included in the total technology package of £240 million over three years is help with Information Technology, Innovation Linked Investment and a provision for extension of Science Parks. It is hoped that this package will particularly benefit the West Midlands.

Other

9. The measures here comprise mainly action on corporate anti-avoidance and personal fringe benefits.

10. On anti-avoidance, the intention is:-

(i) to counter the "British Leyland" device for avoidance through group relief. Treasury Ministers are satisfied that the proposals will not hamper genuine business transactions.

(ii) to legislate on tax havens but not implement the new measures before 1984, and to provide for Double Taxation Relief to be allowed from the same date against the full corporation tax liability before ACT is deducted. This is one of the

changes most widely requested in representations on our corporation tax green paper. Taken together the two changes do not involve any net increase in the burden of tax on international business, but a switch in the burden away from those who remit profits to the UK towards those who accumulate surplus cash balances in tax havens overseas. The tax havens element in the package has been the subject of extensive consultation by Mr Wakeham: he and the Chancellor are satisfied that the proposals in their latest form meet every reasonable representation that has been made during the consultative process.

11. On fringe benefits, the intention is:-

(i) from 1984/85, to increase car and car fuel scales for company cars used privately by higher paid employees by 15 per cent on average. (But the scales will still be well below any realistic estimate of the costs of running a car.)

(ii) on Directors PAYE tax, to deal with cases in which close companies pay directors or higher paid employees a sum without deduction of tax from him and so account for insufficient tax to the Revenue. To do this, tax accounted for by the company will be deemed to be a benefit in kind to the director.

(iii) to tax as a benefit expensive accommodation provided by companies to employees.

(iv) a deficiency in the present rules will be remedied to prevent employees getting both tax relief up to the limit on a commercial mortgage and the benefit of a commensurate interest free loan from the employer for house purchase.

Several other proposals go in the opposite direction:-

(i) the extension from 20 per cent to 30 per cent of the CTT reliefs for minority holdings in unquoted companies, and for let land.

(ii) the removal of the special "deemed domicile" CTT rule applying to those emigrating to the Channel Islands and the Isle of Man. (The Home Secretary has pursued this case for some time.)

(iii) allowing the tenant self-employed (publicans and farmers) to have interest relief on "second" home mortgages.

Specific Duties

12. These will be increased generally in line with inflation, thought with some small real decreases in cigarettes, petrol and derv, and, largely due to rounding, some small real increases in beer, cider and VED. The Chancellor's minute to the Prime Minister of 24 February set out details of the proposals for petrol, derv and VED.

Oil

13. The Chancellor's minute of 4 March reports on the package of measures agreed with the Secretary of State for Energy.

FROM: JILL RUTTER
DATE: 7 March 1983

PS/MINISTER OF STATE (R)

cc PS/Chief Secretary
PS/Financial SEcretary
PS/Economic Secretary
PS/Minister of State (C)
Mr Moore
Mr Robson
Mr French

PS/Inland Revenue

DEVELOPMENT LAND TAX: DISPOSALS OF DEVELOPMENT LAND BY NON-RESIDENTS

The Chancellor has seen your minute of 4 March. He agrees with your Minister's view that we should proceed as already recommended.

JR

JILL RUTTER

BUDGET SECRET

FROM: E P KEMP
7 March 1983

CHANCELLOR OF THE EXCHEQUER

cc Chief Secretary
Financial Secretary
Economic Secretary
Minister of State (C)
Minister of State (R)
Sir Douglas Wass
Sir Anthony Rawlinson
Mr Burns
Mr Middleton
Mr Bailey
Mr Cassell
Mr Moore
Mr Hall
Mr Ridley
Sir Lawrence Airey (IR)
Mr Fraser (C&E)
Professor Walters No 10

BUDGET - FURTHER PROGRESS REPORT ON FISCAL PROPOSALS

I attach a further Progress Report for consideration of the seventh "Overview" meeting tomorrow morning. This is the same Report as you saw late last week. It comprises an overall summary of where we are, detailed tables on the "packages", and a commentary on some of the individual measures.

2. These tables summarise what I hope can be regarded as the near final position on the Budget overall. They are, however, still subject to change, or risk of change, from three main angles :-

a. The actual arithmetic still requires updating in some places (for instance the figures entered for car and car fuel scales in Annex B are actually for the previously suggested 14 per cent average increase; they need to be increased for the 15 per cent now settled.) There may be other points of correction within agreed decisions that also seen to be picked up.

b. Some policy issues are still outstanding. I understand, for instance, that there is a proposal to advance the start of the BES from 1 April 1984 to 1 January 1984. This would have a cost. Another outstanding point,

though this time with as I understand it no cost, is the MST(R) proposal on the question of extending the carry back of ACT. I am not aware of any other outstanding points; if there are any they could perhaps be mentioned at the meeting tomorrow.

c. Changes could of course be necessitated by events in the oil price area this week (or even on Monday of next week). On this you had minutes from Sir Anthony Rawlinson and Mr Cassell of 4 March.

3. Finally, of course, for completeness - I hope only for that reason - I could mention that it is always possible to review or reopen some of the proposals shown below, even if we have regarded them as firm, if now the total picture can be seen it is felt it wants amending in some way.

4. I would suggest that the Overview meeting tomorrow might cover three broad areas :-

a. To note the overall position reached.

b. To clear up any known outstanding points.

c. To discuss on a contingency basis what might happen if the price of oil did make some reductions necessary over the next few days.

5. On the first of these, the meeting might just like to note what it set out in the attached tables. The general shape of the Budget, as we knew, is one in which the lion's share goes to individuals in the first place, though the position alters a little if one brings in to the reckoning one half of the NIS reduction that was announced in the Autumn, and notes that some of the measures scored to individuals particularly in "Housing and Home Ownership" also help the construction industry.

6. On the second point the only two matters I am aware of that are outstanding are those mentioned at paragraph 2(b) above. As I say, if there are any others perhaps they could be mentioned at the meeting. In principle it is undesirable to add to the cost of the Budget following the settlement (at last week's Overview meeting) of the forecasts/PSBRs/fiscal adjustment picture for the FSBR. But it may be that small changes that do not alter the picture materially might be acceptable if there were strong reasons for them.

7. On the third point you have, as I say, minutes from Sir Anthony Rawlinson and Mr Cassell. It is difficult to come to any firm decision about what might be done, since the situation in which something might be necessary has not yet arisen. But it seems sensible to assume that if the size of the Budget does have to be cut down in a hurry it is best to go for measures which are (a) not yet announced and (b) fairly big in themselves - we do not want to try to pick up large sums of money in penny packages. This really reduces the possibility to those which are listed in Mr Cassell's paragraph 5; NIS, personal allowances, Mortgage Interest Relief ceiling, oil, child benefit and enveloping; plus, if revenue increases are to be looked for, action on the indirects of which petrol is the most obvious. On the other side, of course, some of the effect of a fall in oil prices could be met by letting the PSBR rise.

8. Since the situation is unclear obviously final decisions cannot be taken. But the meeting might like to discuss (a) whether these possibilities are all that could be reasonably looked if it was necessary to take urgent action, or whether there are any others which should be pursued, (b) how these various possibilities would rank one against each other if the need for action did come up, (c) possible practical difficulties, eg with the (FSBR, Press Notices, Revenue and Customs publications) and (d) whether there is any more work which can usefully be put in hand now?

EPK

E P KEMP

£ million

	1983-84 PSBR	1983-84 REVENUE	1984-85 PSBR	1984-85 REVENUE
Individuals				
Personal Allowances	1010	1170	1060	1490
Housing and Home Ownership (Table B1)	80	115	65	105
Social Security (Table B2)	75	125	190	320
Unemployment (Table B3)	25	55	40	75
	1190	1465	1355	1990
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Corporation Tax	35	40	60	70
National Insurance Surcharge	200	220	300	400
Small Firms and Enterprise (Table B4)	25	35	130	165
Technology and Innovation (Table B5)	30	40	50	80
	290	335	540	715
North Sea Oil	105	120	85	100
Specific Duties	(10)	(10)	(10)	(10)
Miscellaneous (Table B6)	-	-	(30)	(45)
GRAND TOTAL	1575	1910	1940	2750

Note 1: The measures include both tax and public expenditure elements. For tax the costs shown are the excess over indexation; for public expenditure the excess over what is already provided in the PEWP.

2: The figures shown are rounded and may still vary marginally. The specific PSBR costs shown for each group of measures is necessarily approximate.

ANNEX B

TABLE 1

HOUSING AND HOME OWNERSHIP

£ million

		1983-84	1984-85	Full Year
1.	Enveloping*	50	nil	-
2.	Mortgage Interest Relief ceiling - increase to £30,000	50	85	60
3.	Improvement grants*	10	10	-
4.	Stock relief: householders part exchange simple scheme	under 1	5	5
5.	Self-employed second home mortgage interest relief	2	5	5
	Revenue costs	52	95	70
	Public expenditure costs	60	10	-
	GRAND TOTAL	112	105	70
	Taken as	115	105	

Note: Items marked * are public expenditure

ANNEX B

TABLE 2

SOCIAL SECURITY

		1983-84	1984-85
			£ million
1.	Abolition of £25,000 limit for CTT exemption on gifts to Charities	under 1	under 1
2.	Deeds of Covenant - increase in ceiling for higher rate		3
3.	Tax relief for staff seconded by companies to voluntary bodies	under 1	under 1
4.	Extension of widow's bereavement allowance	25	30
5.	Raise cut-off for SB resources to £3,000 *	2	7
6.	Raise cut-off for SB single payments to £500 *	1	3
7.	Real increase in therapeutic earnings limit *		
8.	New mobility supplement for War Pensioners *		
	Less housing benefit savings	(2)	(6)
9.	Restoration of 5 per cent abatement in UB *	22	59
10.	Increase child benefit to £6.50 per week, plus corresponding rise in one parent benefit *	74	212
11.	Removal of invalidity trap *	4	14
	Revenue costs	25	34
	Public expenditure costs	101	290
	GRAND TOTAL	126	324
	Taken as	125	320

* Public expenditure items. Costs are those over and above amounts provided for in the White Paper

UNEMPLOYMENT

£ million

	1983-84	1984-85
DHSS early retirement (automatic credits 2, long-term SB 22)*	24	24
Enterprise allowance: cash limited nationwide scheme, plus spill over (gross)*	25	25
Part-time JRS from 62*	5	25 †
GRAND TOTAL	54	74
Taken as	55	75

Note: Items marked * are public expenditure

† £25 million is provisional estimate

ANNEX B

TABLE 5

TECHNOLOGY AND INNOVATION

£ million

		1983-84	1984-85	1985-86
1.	Extension of transitional period for capital allowances - films	nil	nil	30
2.	Extension of transitional period for capital allowances - teletext TVs	nil	10	15
3.	SEFIS*	20	40	40
4.	Information technology*	5	8	11
5.	Innovation linked investment*	5	15	20
6.	Advisory services*	9	6	6
7.	Science Parks* (included above)			
	Revenue costs	nil	10	45
	Public expenditure costs	39	69	77
	GRAND TOTAL	39	79	122
	Taken as	40	80	

Note: Items marked * are public expenditure

The cost of the whole package over three years is £240 million

SMALL FIRMS, ENTERPRISE AND WIDER SHARE OWNERSHIP

£ million

		1983-84	1984-85	Full Year
1.	Business Expansion Scheme	nil	75	75
2.	Loan Guarantee Scheme*	nil	nil	-
3.	Wider share ownership	20	30	40
4.	Capital Gains Tax (see note 1)			
	a. monetary limits	nil	1	1
	b. retirement relief	nil	1	4
5.	VAT registration thresholds	5	10	10
6.	De minimis limit for assessment of apportioned income	under 1	under 1	under 1
7.	Acceptance credits	1	1	1
8.	Capital Transfer Tax (see note 2)	8	18	20
9.	Zero/deep-discounted stock	neg	15	15
10.	Relief for interest, employee buy-outs	1	1	2
11.	Tax treatment of interest paid by companies to non-residents	under 1	under 1	10
12.	Increase in proportion of office space qualifying for industrial building allowance	nil	10	25
13.	DLT - extension of own-use deferment	nil	under 1	4
14.	Small Workshop Scheme - averaging for converted premises	under 1	under 1	under 1
	GRAND TOTAL	36	163	208
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Note: Items marked * are public expenditure

1. The cost of these CGT measures when statutory indexation is added is nil, 5 and 15 million.

2. Indexation of CTT costs 15, 30 and 45 respectively. The additional costs shown for item 8 are for rounding up the indexed thresholds, for extending the instalment period from 8 to 10 years, and for increasing reliefs on let land and unquoted companies to 30 per cent.

MISCELLANEOUS

£ million (yields)

		1983-84	1984-85	Full Year
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2.	Cheap housing for directors	nil	nil	(1)
3.	Life assurance: chargeable events: secondhand bonds	under (1)	under (1)	under (1)
4.	CGT: non-resident trusts	under (1)	under (1)	under (1)
5.	CTT: remove special deemed domicile rule for Isle of Man etc	1	2	2
6.	Group relief: avoidance (BL)	nil	(10)	(10)
7.	DLT: disposals by non-residents	(1)	(2)	(2)
8.	Taxation of international business. Offset by Double Taxation Relief against Corporation Tax	nil	nil	nil
9.	Beneficial mortgage loans from employers	nil	under (1)	under (1)
10.	Directors PAYE tax	nil	(10)	(10)
11.	TSBs to be treated as bodies corporate	3	10	10
	GRAND TOTAL	2	(47)	(52)
	Taken as	-	(45)	

Annex C.

INDIVIDUAL MEASURES

Personal Allowances

1. All thresholds and allowances (including the higher rate and IS thresholds) to increase by 14 per cent, or 8½ per cent above the statutory minimum. This will for the great majority of people (but not quite all) more than outweigh the increased National Insurance Contributions which come into effect in April.

Social Security etc.

2. Child benefit to increase to £6.50 per week, taking its value above the level inherited in 1979. There will be a parallel increase in one-parent benefit. The 5 per cent abatement in unemployment benefit, effected in 1980, to be restored; widows bereavement allowance to be extended to a second year; the invalidity trap to be eliminated. Should go some way to offset the criticism on general social security upratings.

Housing and Home Ownership

3. This group includes the increase in the Mortgage Interest Relief ceiling from £25,000 to £30,000. Also included are proposals to provide more for Home Improvement Grants, and also to provide money for so-called "enveloping" schemes, under which local authorities repair the external fabrics of complete streets or terraces, as part of helping counter the problems of housing decay.

Unemployment

4. The measures here include proposals in respect of early retirement, a nationwide extension of the Enterprise Allowance Scheme, and making the Job Release Scheme available to part-timers from the age of 62.

Corporation Tax

5. Reduce the small companies rate from 40 per cent to 38 per cent, and alter the limits so as to reduce the transitional marginal rate.

National Insurance Surcharge

6. Cut NIS by ½ per cent for the private sector only, from next August. Complete abolition of the Surcharge is the single measure most frequently and forcefully pressed in industrial representations.

Small Firms, Enterprise and Wider Share Ownership

7. A major extension and simplification of the Business Start-Up Scheme, to be called the Business Expansion Scheme. The principal change is the extension of the present scheme to provide tax relief for equity investment not just in new companies but in all qualifying established unquoted trading companies. (Following a review, other changes are being made to make the scheme less restrictive.) Also further measures to encourage wider share ownership, improvements in the Capital Transfer Tax regime, an extension of the Loan Guarantee Scheme, and an increase in the VAT registration threshold.

Technology and Innovation

8. The major measure is the re-opening, at a cost of £100 million over the next three years, of the Small Engineering Firms Investment Scheme (SEFIS). Also included in the total technology package of £240 million over three years is help with Information Technology, Innovation Linked Investment and a provision for extension of Science Parks. It is hoped that this package will particularly benefit the West Midlands.

Other

9. The measures here comprise mainly action on corporate anti-avoidance and personal fringe benefits.

10. On anti-avoidance, the intention is:-

(i) to counter the "British Leyland" device for avoidance through group relief. Treasury Ministers are satisfied that the proposals will not hamper genuine business transactions.

(ii) to legislate on tax havens but not implement the new measures before 1984, and to provide for Double Taxation Relief to be allowed from the same date against the full corporation tax liability before ACT is deducted. This is one of the

changes most widely requested in representations on our corporation tax green paper. Taken together the two changes do not involve any net increase in the burden of tax on international business, but a switch in the burden away from those who remit profits to the UK towards those who accumulate surplus cash balances in tax havens overseas. The tax havens element in the package has been the subject of extensive consultation by Mr Wakeham: he and the Chancellor are satisfied that the proposals in their latest form meet every reasonable representation that has been made during the consultative process.

11. On fringe benefits, the intention is:-

(i) from 1984/85, to increase car and car fuel scales for company cars used privately by higher paid employees by 15 per cent on average. (But the scales will still be well below any realistic estimate of the costs of running a car.)

(ii) on Directors PAYE tax, to deal with cases in which close companies pay directors or higher paid employees a sum without deduction of tax from him and so account for insufficient tax to the Revenue. To do this, tax accounted for by the company will be deemed to be a benefit in kind to the director.

(iii) to tax as a benefit expensive accommodation provided by companies to employees.

(iv) a deficiency in the present rules will be remedied to prevent employees getting both tax relief up to the limit on a commercial mortgage and the benefit of a commensurate interest free loan from the employer for house purchase.

Several other proposals go in the opposite direction:-

(i) the extension from 20 per cent to 30 per cent of the CTT reliefs for minority holdings in unquoted companies, and for let land.

(ii) the removal of the special "deemed domicile" CTT rule applying to those emigrating to the Channel Islands and the Isle of Man. (The Home Secretary has pursued this case for some time.)

(iii) allowing the tenant self-employed (publicans and farmers) to have interest relief on "second" home mortgages.

Specific Duties

12. These will be increased generally in line with inflation, thought with some small real decreases in cigarettes, petrol and derv, and, largely due to rounding, some small real increases in beer, cider and VED. The Chancellor's minute to the Prime Minister of 24 February set out details of the proposals for petrol, derv and VED.

Oil

13. The Chancellor's minute of 4 March reports on the package of measures agreed with the Secretary of State for Energy.

FROM: MISS J M SWIFT
DATE: 7 March 1983

~~PPS~~

Chief Secretary
Sir Douglas Wass
Sir Anthony Rawlinson
Mr Burns
Mr Middleton
Mr Byatt
Mr Littler
Mr Bailey
Mr Mountfield
Mr Cassell
Mr Kemp

BUDGET: PUBLIC EXPENDITURE CUTS TO OFFSET LOWER OIL PRICES

The Chief Secretary has seen and broadly agree with Sir Anthony Rawlinson's minute of 4 March to the Chancellor.

2. But he thinks that, if PSBR reductions are needed and it is tight on the revenue side, it would be worth considering omitting some of the new measures to be announced in the Budget and reducing the Contingency Reserve correspondingly.

MISS J M SWIFT

BUDGET CONFIDENTIAL

From: P Mountfield
Date: 7 March 1983

PCWP

Chancellor of the Exchequer

cc -

Chief Secretary
Minister of State(C)
Sir Anthony Rawlinson
Mr Wilding
Mr Kemp
Mr Moore
Ms Seammen
Mr Traynor
Mr King - UPPS

+ W.S.C!

C

A pity. I expected more than x. If x is right, we can drop the paragraph in the speech!

GH

MANPOWER EFFECTS OF THE BUDGET

You asked for a note.

2. We estimate the overall effect at about +30. In more detail:

a. Customs a negligible requirement for additional staff, which can be absorbed within existing ceilings.

b. Inland Revenue. On present information, net savings of 50-100. But Inland Revenue believe that they will need to retain these staff, and argue that they have already received assurances that they may do so. We have yet to examine their case, and will report further when it is received if there are problems.

c. DHSS. The various measures require a net addition of 347, after allowing a saving of 30 from the employment measures. But DHSS have about 280 staff to spare within their totals, from the original Autumn proposals. The net extra is therefore only 70 which we think they can absorb.

d. Employment (Including MSC). There is a net +30, offset by a reduction of 30 in DHSS which is taken into account in the figures above.

3. So, overall, the +30 is the worst case: if we can persuade Inland Revenue to disgorge the savings which we believe they can achieve, this will turn into a -20 to -70. To put this in context, the overall estimates figure for 1 April 1984 is 628317. The Budget changes are therefore well within the margins of error.

PM

P Mountfield

Clean type M.

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

JOU:
Try this on ~~[illegible]~~ FP etc. And no doubt try your own informants (Sutherland)

PRIME MINISTER

INCOME TAX THRESHOLDS

You asked me to think about the possibility of increasing the thresholds by 10 per cent.

2. In recent weeks I have, as you know, been planning a 8½ per cent increase, largely because:-

a. we need to demonstrate our determination to go on reducing borrowing, , even if only at a moderate rate; this which means a 1983-84 PSBR which can be shown (after some "rounding down") as no more than £8 billion;

b. which in turn means that our scope for ~~net~~ total tax reductions (after indexation and valorisation) is, on the latest forecast, limited – in terms of PSBR impact ~~this year's PSBR~~ – to some £1.5 billion (and even that is pushing it a bit); and

c. to target more than three quarters of these reductions on individuals, rather than business and industry - and more than two thirds on the single area of income tax thresholds - would be open to sharp criticism. (Frankly, I think we would be accused of electioneering.)

3. There is no

3. There is no particular magic about the 8½ per cent figure: the £1 billion relief (in PSBR terms) which it represents, on top of indexation, is more important. But 8½ per cent does meet, or beat, a number of important targets, viz:-

a. taking the Government Actuary's assumption of earnings growth of 6½ per cent between 1982-83 and 1983-84, it reduces or matches average rates of tax and NIC for 1982-83 for all people who are contracted-in;

b. it reduces average rates of tax compared to 1978-79 for married men on at least three quarters of average earnings - ie two thirds of married men; and

c. because I have rounded up the married man's allowance, it gives all married men a tax reduction of just over £2 a week.

4. As I told you, indexation plus 10 per cent would restore personal allowances to the same percentage of average earnings as in 1978-79 and 1979-80. But that would not silence those who criticise the rising tax burden. They would say - with some justice - that a fair comparison should take account of NIC, and of the movement in prices since 1979-80. We would have to go to 13 per cent over indexation in order to be able to claim that we had restored the allowances to their 1979-80 levels in terms of prices. To get back to 1978-79 levels, taking account

/also of NIC, would

4. As I told you, there is a huge ~~variety~~ choice of figures on which to base alternative calculations. They are all ~~[illegible]~~ complicated by two things: ~~[illegible]~~ the increases in NIC which we have had to make (including this year's special addition to the contracted out rate) i.e. a total of [ ] per cent for those contracted in, and of [ ] per cent for those contracted out; and the very large increase in average earnings that ~~has~~ taken place.

5. With this ~~in~~ mind one can make ~~[illegible]~~ (a variety of) comparisons with 1978/79, Labour's last year. ~~[illegible]~~ A reduction in the average (rate of (percentage) tax and NIC combined to the levels in that year would require an increase of more than 30 per cent over indexation. On average rates of tax alone, indexation plus 8½ per cent restores the position for most married men, but indexation plus 15 per cent ~~is~~ (would be) needed ~~at least~~ to match 1978/79 for a majority of the single (and earning wives).

6. The figure of indexation plus 10 per cent (which I mentioned) would, as it happens, restore allowances to their 1978/79 level as a percentage of earnings. But ~~[illegible]~~ ~~particular~~ (it would take no particular tricks, since that) milestone is ~~very~~ seldom ~~referred to~~ mentioned. ~~Not surprising.~~ ~~[illegible]~~ Reference is more often made to the real value of the allowances expressed (as "Rooker-Wise" requires) in terms of prices; and by that yardstick indexation plus ~~4~~ 3 per cent is ~~enough~~ sufficient to restore the 1978/79 level. (I see that the IFS Budget

Factbook, for example, suggests that to "provide complete indexation during my [his] time as Chancellor" would require me to make an overall increase this year of 12 per cent (and

[illegible] we shall be doing better than that.) Average earnings, of course, will have done much better still – which means that all the options, including basic indexation, show real net earnings in 1983/84 after tax and NIC as higher than in 1978/79.

7. There is one other thing ~~way of looking at~~ ~~all this~~ which may have been obscured by the way in which we are obliged to do our initial arithmetic, in terms of the first year net PSBR cost of any measure. The income tax cuts which I now propose cost, on that basis,

"only" £1 b million. But the full year ~~total reduction of~~ revenue cost of ~~the~~ income tax cuts, including indexation, is about £2.5 billion, ~~or the extra 1½ pence~~ and that is the figure which will hit the headlines.

8. I believe it would be unwise to go beyond that, not least because it would raise the PSBR by

~~also of NIC, would require an increase of more than~~ 30 per cent over indexation. Even to ensure that no-one's tax and NIC payments rise between this year and next would require 14 per cent over indexation.

5. I agree that the picture is depressing: it arises because we had to forego any increase in allowances in 1981, and have had to increase NIC every year. But the milestones we would have to reach in order to defuse the criticisms with which you are concerned are frankly unattainable in this Budget, and going to the 10 per cent ~~milestone would satisfy none of these critics.~~

~~6. But it would I think touch off new, and different~~ criticisms, from our own side and in the markets. For accommodating the extra costs (£130 million next year) would mean either paring other Budget plans, including ~~the further help I envisage for business and industry,~~ ~~or settling for a PSBR rounded~~ to £8.5 billion. To announce an intention of borrowing more, in nominal terms and as a proportion of GDP, next year than in the current year would cause considerable surprise, since it would be inconsistent with the strategy we have been following over the years. And it would reduce ~~still~~ still further our ~~very limited~~ very limited room for manoeuvre

in face of a sharp fall in oil prices.

7. So I really do think that 8½ per cent makes sense, and that more would be a mistake.

G.H.

7 March 1983

PPS/CHANCELLOR

file no TEB/HA/10

Chancellor

copied to:

Mr Salveson (for transmission to No.10)
PS/CST
PS/FST
PS/EST
PS/MST(C)
PS/MST(R)
PS/Home Secretary
PS/Lord Chancellor
PS/Foreign Secretary
PS/Secretary of State for Education and Science
PS/Lord President of the Council
PS/Secretary of State for Northern Ireland
PS/Secretary of State for Defence
PS/Minister of Agriculture, Fisheries and Food
PS/Secretary of State for Environment
PS/Secretary of State for Scotland
PS/Secretary of State for Wales
PS/Lord Privy Seal
PS/Secretary of State for Industry
PS/Secretary of State for Social Services
PS/Secretary of State for Trade
PS/Secretary of State for Energy
PS/Secretary of State for Transport
PS/Chancellor of the Duchy of Lancaster
PS/Secretary of State for Employment
PS/Paymaster General
and officials in HMT, Revenue Departments and other Departments in Whitehall

TREASURY BRIEF

I attach the latest version of this Brief. Changes from the previous Brief, of 28 February, are sidelined. Next week's Brief will be the last before the 15 March Budget; briefing on the Budget will be made available separately in the usual Budget Brief. Parts of this will be incorporated in the next subsequent weekly Brief to be finalised 21 March.

M M Deyes

M M DEYES

RA

R I G ALLEN

7 March 1983

EB Division
H M Treasury
01-233-5503

ECONOMIC BRIEF: CONTENTS — SOURCES

A GENERAL ECONOMIC STRATEGY

1. Government's main economic objectives

Main objectives are to achieve, over a period, a sustained improvement in the economy through reduction of inflation, lower interest rates and promotion of enterprise and initiative. Policies will continue to be applied to these ends.

2. Control of public spending: TSCS unimpressed?

[1983 Public Expenditure White Paper Cmnd 8789 published 1 February. TSCS comments published 3 March. Debate scheduled for Wednesday 9 March.]

Government values Select Committee's comments and will examine them carefully. But no justification for implication that public expenditure plans have not been substantially reduced. No doubt that, compared with earlier plans, plans for future (cash) expenditure have been substantially reduced (by £1.1 billion in 1983-84 and by £1.2 billion in 1984-84). True that Government's success in reducing the rate of inflation means that the available cash will now go further. That should be warmly welcomed and in no way detracts from fact that previous plans were reduced. Really important achievement is that ratio of public expenditure to gross domestic product - best measure of burden which public expenditure places on rest of economy - is now planned to fall. (See also Section K.)

3. Current indicators suggest recovery over/activity flat?

Output measure of GDP rose ½ per cent in year to 1982 Q4, and is 1½ per cent higher than in spring 1981. True that manufacturing output declined during 1982 but this partly reflected external developments: volume of world trade fell substantially, contrary to expectation at time of 1982 Budget. And latest CBI Enquiry (see B6) considerably more optimistic about prospects for manufacturing. Modest growth in GDP and manufacturing expected in 1983. Await Budget forecast for full assessment of outlook.

4. Is Government strategy still on course?

Yes. UK monetary and financial conditions remain sound. Government spending and borrowing on target - as is monetary growth. Inflation is falling. Underlying industrial performance also improving eg productivity, competitiveness. UK had substantial current account surplus last year (but see G3). Foreign currency debts almost halved since took office. Movement in sterling needs to be considered in context concern about oil prices and of strength of other currencies eg $.

TCSC
- public spending

5. Exchange rate slide will improve external competitiveness?

Will only have lasting benefit if wage settlements continue to be contained at more moderate, and realistic levels. Keeping firm control of labour costs is the key to improving our competitive position. Past experience (eg 1967-72 and 1973-76) illustrates all too clearly how easy it is for immediate benefits of devaluation to be eroded through higher price and wage inflation. (See also F5 and G10 on competitiveness.)

6. TUC argument that lower pay settlements reduce demand and jobs

Depends on Government's policy stance. It will not be true if Government sticks to its monetary targets. For a given money supply, lower wages and prices make room for higher real demand and output. Lower inflation stimulates demand both through 'real balance' effect on consumer spending and through beneficial effect of lower wages on trade competitiveness; and because lower prices make room for lower interest rates, which will help company cash flow and spending.

7. Oil price uncertainties and implications for Budget/UK economy?

Await Budget. (See also Section S.)

8. Outlook for Budget/Fiscal adjustment?

Await Budget. (Other fiscal policy points, see Section H.)

9. What about CBI Budget representations?

[CBI proposals published 26 January 'Costs are Crucial', include in £4 billion programme abolition of NIS, lower business rates, extra capital expenditure, lower energy costs and indexation of personal taxes (but not specific duties); CBI say this is possible within £9 billion PSBR for 1983-84.]

CBI views always carefully studied. All representations play a useful part in putting together a Budget. Views of national organisations like CBI particularly important. But cannot anticipate Budget decisions.

10. TUC Budget representations? Meeting to discuss?

[£10 billion Budget package in TUC Economic Review 1983 published 2 February, presented as first stage in five year programme of expansion linked to national and company level planning and accompanied by exchange controls, selective import controls and NEA.]

Chancellor always listens carefully to TUC views. All representations play a useful part in putting together a Budget, and views of national organisations like the TUC are particularly important. But cannot be expected to agree with TUC criticisms of general thrust of Government policy.

11. Labour Party programme

[Observer 20 February reports discussions in progress on drafting manifesto to be ratified (according to The Times 17 February) on 24 March. Possible that Labour Party, or Shadow Chancellor, may publish 'alternative Budget' before 15 March.]

Defects of Labour programme remain. Blow to confidence; wage restraint assumed without specific mechanism to achieve; 'planned trade' proposals equally vague. Claimed validation by running programme through Treasury models does not make results definitive. Note that LBS (21 February) assessment of Labour Party policies says: 'If unions and financial markets act to support these policies, then unemployment falls by about 1/3 million and inflation reaches only (sic) 11 to 12 per cent. If not, then unemployment rises slightly as inflation accelerates to around 17 per cent'.

12. Alliance programme a more credible alternative?

Latest Alliance document not entirely consistent with earlier public pronouncements and fudges the difficult decisions. Full year cost of proposals ~~more~~ (perhaps some £6-7 billion) nearly twice what was previously claimed to be sufficient to achieve similar cut in unemployment. Implied increase in PSBR to 4 per cent of GDP next year Liable to cause anxiety in markets. Tax cuts' effect on inflation only short term -yet no mention of earlier ideas on incomes policy to prevent resurgence of inflationary pressures. Monetary and exchange rate policy only vague aspirations.

13. Conservative traditionalists not behind Government policy?

[Sir Ian Gilmour's book 'Britain Can Work' published 3 March.]

Note that Sir Ian hopeful of another term of Conservative Government. We share his concern about unemployment - witness our measures to ameliorate worst effects - but convinced sounder economy we are in process of promoting by our current policies is only long term source of substantable employment.

Dried
psicce

BULL POINTS As at 7.3.83

(i) Activity. GDP has recovered by 1½ per cent since spring 1981. Industrial output in the fourth quarter of 1982 was 2 per cent above its trough in the second quarter of 1981 (largely oil and gas). More immediate indicators for manufacturing sector (business confidence, order books etc) more encouraging. Recent forecasts continue to see prospect of modest recovery this year.

(ii) North Sea oil and gas extraction at record level in 1982 Q4.

(iii) Demand: Consumers' expenditure in the fourth quarter was 1½ per cent up on the preceding quarter and in 1982 as a whole, 1 per cent higher than in 1981. Retail sales, rose by 1½ per cent in 3 months to January on preceding 3 months. New car sales highest for any January and import penetration down.

(iv) PSBR: government borrowing now amongst lowest in industrialised world.

(v) Public expenditure planning total for 1983-84 below total published at Budget time and about £½bn below planning total announced in Autumn Statement.

- first time since 1977 that a Government has not increased its spending plans in course of Survey

- fall in ratio between public expenditure and GDP from 44½ per cent in 1981-82 to 44 per cent in 1982-83 (expected outturn) should fall again to 43½ per cent in 1983-84.

(vi) Prices. Increase in RPI over the 12 months to January was 4.9 per cent; the rate of inflation has now fallen for eight consecutive months and is the lowest since February 1970. Government forecast of 5 per cent inflation by early 1983 achieved. 12-monthly increase in wholesale output prices (7.1 per cent in February) is lowest since July 1973.

(vii)

Latest CBI trends enquiry shows sharp swing in balance of firms expecting manufacturing output to increase from -5 to +8. Biggest single positive swing since January 1981.

(viii) Manufacturing productivity. Output per head has risen about 12½ per cent since end 1980. Output per head and output per hour now about 5 and 9 per cent higher than previous cyclical peak in 1H 1979.

(ix) Competitiveness. Cost competitiveness (manufacturing) improved by around 25 per cent since early 1981.

(x) Industrial stoppages. Total number of working days lost in 1982 (7.9 million) well below average of 12 million of previous 10 years. Very few days lost in private sector.

(xi) Profits: Industrial and commercial companies' gross trading profits (net of stock appreciation, exluding North Sea) up 14 per cent in first 3 quarters of 1982 on average 1981 level. [NB recovery in profits from very low base: pre-tax real rate of return of ICC's (excluding North Sea) only 3 per cent in 1981.]

(xii) Controls: HP controls abolished in summer, adds to a long list of other controls already abolished (pay, dividends, prices, exchange controls, office development permits, industrial development certificates).

(xiii) Enterprise zones: further 13 zones announced in 1982 bringing total to 24.

(xiv) Housing starts (total) - up over 13 per cent in 3 months to January on previous 3 months. [NB But broadly flat during 1982.] New construction orders up 8% in Q4 1982 compared with same period of 1981.

(xv) Total new construction work: in third quarter of 1982 was 6 per cent higher than in the previous quarter and 7 per cent higher than the same period a year earlier while total construction output was 3 per cent and 2 per cent up on similar comparisons.

(xvi) Special employment measures. Total planned provision for special employment schemes £1½ billion in 1982-83. Further measures announced end-July - new community work programme (started October), job splitting subsidy schemes (from January 1983); total planned provision for 1983-84 £2 billion.

(xvii) Overseas debt repayments. Official external debt reduced from $22 billion in May 1979 to less than $12¾ billion at end-December 1982.

(xviii) Civil service now 652,500 (1 January 1983) - re
Government took office. On target to achieve smallest C
(630,000).

Housing starts

(xix) Owner occupation at highest ever level: 56 per cent of

Economic Briefing Division, HM Treasury, 01-233 5514/5503

B ECONOMIC ACTIVITY AND PROSPECTS

1. Recent GDP figures

[GDP (O) the best short-term indicator of the three GDP measures - rose slightly in 1982 Q4, confirming a gently upward trend since 1982 Q1; level now about 1½ per cent above 1981 Q2 trough (largely attributable to increased North Sea production). Evidence of declining trend in manufacturing during 1982. Industrial output in 1982 Q4 1½-2 per cent above 1981 Q2 trough - virtually all extra North Sea oil output; manufacturing output 2 per cent below 1981 Q2.]

GDP has recovered 1½ per cent since spring of 1981, and industrial output has recovered 2 per cent. Now further signs that output picking up in some sectors - including some in manufacturing. More immediate indicators - manufacturing order books, business confidence, optimism on output prospects - all encouraging (see B6 below on CBI Survey). Prospect of modest recovery in 1983. Sounder base being prepared - by lower inflation and interest rates, higher productivity etc - for expansion in medium term.

2. Hasn't UK suffered worst collapse of any major industrialised country since 1979?

[On Treasury estimates, between 1979 and 1982 UK GDP fell by just over 4 per cent; US fell ½ per cent and Canada 2 per cent. In Germany GDP has been roughly constant and in Japan, France and Italy it rose].

UK GDP grew relatively slowly throughout post-war period. But our performance during 1982 was better than many of our competitors.

3. Manufacturing production in 1982 Q4 returned to 1967 levels?

Such long term comparisons inappropriate without recognising changing sectoral composition of output. As consumers' preferences change and balance of comparative advantage alters, so will pattern of output. GDP is almost 26 per cent above its level in 1967.

4. Prospect for UK economy

[Industry Act Forecast Tables summarised in Commentary - Z7. NB New forecast with Budget 15 March; undue emphasis should not be given to precise numbers in IAF.]

Prospect for 1983 remains one of modest recovery - most outsi
of some 1½-2 per cent in 1983 - and continuing moderate infl
published on 15 March with Budget. (Outside Forecasts: See B

Output

5. Other evidence of improvement in economy?

See Bull Points (following Section A).

6. Latest CBI assessment in February Trends Enquiry?

[See Commentary - Z7 - for details.]
Latest Enquiry results encouraging, in particular sharp swing in balance of firms expecting manufacturing output to increase - biggest positive swing since January 1981. Order books have also improved substantially. Strengthening of output expectations seems to reflect both smaller proportion of firms who believe stocks excessive and growth in demand, especially for consumer goods.

7. New orders figures and short-term indicators now more encouraging?

[See Commentary - Z6 - for latest indicators.]

Figures were manifesting depressed economic activity partly reflecting flatness in world trade, but more recently some encouraging signs (e.g exports and total order books in CBI Enquiry (February), engineering and new construction orders). Conjuncture of more immediate indicators now a little more encouraging than 2-3 months ago.

8. Construction industry forecasts show prospects of modest recovery?

[Joint Forecasting Committee of industry's 'Little Neddy' published 6-monthly forecast on 15 December. Prospect is for modest recovery in three years to 1984 - although output not restored].

Construction industry's problems remain difficult, but forecast moderately encouraging and recovery in housing investment in 1983 (some 16-17 per cent) very encouraging. Improved outlook for construction reflects success of policies reducing inflation and interest rates.

9. Recent private investment performance?

[For latest available statistics see Commentary - Z3.]

Manufacturing investment has been weak (fell 8 per cent, including leased assets, in 1982) but more than offset by increase in investment in distributive and service industries (up 6 per cent). Housing starts and new construction orders also encouraging. [IF PRESSED: latest DOI investment intentions survey suggesting 3 per cent fall in manufacturing investment between 1982 and 1983 is undoubtedly disappointing; outlook for total private fixed investment more encouraging].

10. Continued destocking threat to recovery?

[For latest statistics see Commentary - Z3.]

Fourth quarter destocking consistent with recent movements in output and demand, and Q4 trade figures (see G2). Stock levels in relation to output still not particularly low, and some more destocking may occur. But latest CBI Enquiry suggests that smaller proportion of firms now believe that stocks (of finished goods) are excessive; this may partly account for improvement in output expectations.

11. Productivity growth falling off?

[Growth in output per head in manufacturing slowed down sharply during 1982; 2 per cent in year to 1982 Q4, compared 10 per cent in previous 12 months.]
Manufacturing productivity gains in last two years impressive - much bigger than might have been expected on past experience. Slow down in 1982 probably inevitable as best opportunities for plant closures and improved efficiency are taken first. Recent experience still better than average post-war experience.

12. CSO's index of leading cyclical indicators?
[January cyclical indicators published 22 February.]

All four of the cyclical indicators when taken together suggest that the economy should continue in the upswing phase through 1983. Shorter leading and co-incident indicators have continued to rise over recent months while longer leader rose to November, and was thereafter unchanged to January.

12. Outside forecasts

[GDP profile in recent major assessments and in IAF:

Per cent change

	Phillips & Drew (Mar)	Simon & Coates (Mar)	NIESR (Feb)	LBS (Feb)	OECD (Feb)	CBI (Nov)	St James (Nov)	IAF (Nov)
1983 on 1982	+1¾	+2¼	+1½	+1¾	+1½	+1¼	+2	1½
1984 on 1983	1½	+¾	+1¾	+2	-	-	+3½	-]

Nearly all major outside forecasts see prospect of continued modest recovery (GDP up 1½-2 per cent in 1983) and consumer price inflation around 6-7 per cent range by end 1983.

Outside
forecasts

C LABOUR MARKET

[NB For latest information on earnings/pay settlements see Section D.]

1. Unemployment figures (new basis)/ other labour market indicators?

[Little change expected in 'headline' total till May. June influx of school leavers will not influence headline total until September/October. Overtime/total hours worked flat in 1982. Short-time fell back slightly in December after increasing steadily since July 1982.

	1982 Q1	Q2	Q3	Q4	1983 Jan	Feb
'Total unemployment' (millions)	.286	2.80*	2.94*	3.07	3.23 (13.8%)	3.20 (13.7%)
UK adult sa unemploment (millions)	2.68	2.74	2.84	2.91	2.98 (12.8%)	3.00 (12.9%)
Increase in period (000s)**	+23*	+28	+31	+27	+33	+32
vacancies (000s)***	112	107	111	115	118	121

*After allowing for over 60's transferring off count
**Differences between consecutive three monthly moving averages
***Only about one-third of vacancies are notified officially. Probably total between 275 and 325 thousand].

Fall in headline total to be welcomed, as is evidence of no further worsening in underlying rate of increase. Underlying trend regrettably still upwards, and will continue so for some time yet, though prospect of modest rise in orders, output etc will improve outlook for employment.

2. Unemployment still rising despite Government's policies?

Excessive wage increases - unjustified by past output/productivity performance - have priced people out of jobs. Deepseated problems will take long time to check and reverse. Essential to build on underlying signs of strength in economy: higher productivity and greater competitiveness.

3. Wage cuts not route to increasing employment?

See A6.

4. Shorter work-time?

[Supported by TUC - also referred to in 1983 Economic Review.]

If reductions in working time to reduce unemployment, must also be a corresponding reduction in incomes. If weekly pay stays constant while hours fall, unit labour costs are increased, competitiveness worsens, output and employment suffer.

Unemployment

5. Unemployment in UK higher than in other countries?

[On standardised definitions in 1982 Q4 UK unemployment was 13.1 per cent (new series) compared with 8.9 per cent 'major 7'. On national definitions UK unemployment more than doubled since 1979 compared with major 7 rise of about three quarters.]

Unemployment has risen sharply in many industrialised countries - increase over year to latest available month in number unemployed (on national definitions - not strictly comparable) was much more in US (23 per cent) and Germany (33 per cent), Holland (37 per cent) and Canada (51 per cent) than in UK (12 per cent).

6. True level of UK unemployment really much higher?

[TUC Economic Review 1983 claims 'true' figure over 4 million; Labour Research Department say 5 million The Times 6 December; SDP say 5¼ million Guardian 7 January.]

Gross exaggerations, relying heavily on assumed one million fall in labour force between 1979 and 1982 and including those benefiting from special employment measures - who are not unemployed. The latter 'adjustment' to official figures clearly inappropriate. While former is not corroborated by most recent statistics. Between 1979 and 1982, small reduction in labour force due to lower 'activity rates' was insufficient to offset increases in population, and labour force grew by ¼ million.

7. Unemployment figures in 1983 PEWP

[Assumed unemployment (on claimants basis) for social security projections (GB, excluding school leavers) average 2.74 million in 1982-83 and 3.02 million thereafter. Figures consistent with those given (on 'registration' basis) in Autumn Statement].

Not a forecast. Assumptions on unemployment are in effect same as in Government Actuary's last report. Only change is definitional, ie from registration to claimant basis. Redefined figures consistent with Autumn Statement unemployment assumptions.

8. Employment continuing to fall?

[Decline in employed labour force (including self-employed) 2.0 million (9¾ per cent) from mid 1979 to 1982 Q3. In 1982 quarterly decline increased - Q1 98,000, Q2 160,000, Q3 200,000 - but series of questionable reliability. Manufacturing employment fell 85,000 in 1982 Q4 compared 94,000 in previous quarter. [Sir T Beckett expects (FT report 4 February) fall of 80-90,000 more jobs in manufacturing over next four months].

Sustainable recovery and improved job prospects requires curbed inflation, greater competitiveness and lower interest rates. Substantial provision (£1½ billion) made available in current year to assist most vulnerable groups (see C12 below).

9. Recent productivity gains inimical to higher employment/lower unemployment?

Probably true in short run. But as experience in Japan and many other countries clearly demonstrates, higher productivity essential for longer term growth and employment opportunities.

10. Revision to past employment figures significantly affect figures of GDP, manufacturing productivity etc?

[Employed labour force mid-1981 on new data about ¾ million higher than previous estimates, of which 550,000 additional employees in employment 215,000 additional self-employed. February Employment Gazette gives regional estimates of new figures on employees in employment published in December Gazette and shows self employed, at 2.1 million in 1981, almost 9 per cent of employed labour force.]

GDP effect probably quite small. Impact on measured productivity - output per head - greater eg manufacturing productivity in 1981 revised down by about one per cent. But will not significantly affect exceptional manufacturing productivity growth over last two years.

11. Cost of unemployment/Effect on PSBR?

Changes in unemployment affect public finances according to underlying circumstances, e.g changes in world trade, UK competitiveness, relative UK earnings etc. Not sensible to talk as if 'cost of unemployment' a single figure. Unemployment and supplementary benefit to people counted as unemployed currently expected to total £5 billion in 1982-83; comparable figures for uncollected taxes and national insurance contributions cannot be given. No basis available to estimate the level of earnings and tax receipts if all unemployed were working.

12. Government concerned over unemployment?

Government pursuit of balanced fiscal and monetary policies, along with lower pay settlements, essential pre-conditions for sustainable increase in employment. Government has substantially increased spending to alleviate impact on especially vulnerable groups. Planning to spend £1½ billion in cash on special employment and training measures in 1982-83 (40 per cent more than in 1981-82) and £2 billion in 1983-84. Latter includes £950 million allocated to Youth Training Scheme and £260 million (gross) to (a) new community programme - designed to provide up to 130,000 places for long term unemployed - and (b) new Job Splitting Subsidy to encourage extension of part time work and provide additional opportunities for productive jobs for unemployed people.(See also Section D).

D PRICES AND EARNINGS

PRICES

1. Inflation rate

[Year on year RPI increase 4.9 per cent in January, compared 5.4 per cent in December].

Year on year rate of inflation again fell sharply in January to 4.9 per cent - lowest level for 13 years (compared 4.9 per cent in February 1970).

2. Prospects for zero inflation?

We shall continue to maintain the sound financial policies which have brought such success so far.

3. Comparison with previous Government?

[Average year-on-year rate of inflation between February 1974 and May 1979 15.4 per cent. Average level of inflation since May 1979 has been 11.9 per cent.]

When previous Government left office (May 1979), year-on-year rate of inflation was 10.3 per cent - and rising (May 1978 figure was 7.7 per cent). Now (January 1983) down to 4.9 per cent.

4. Higher RPI inflation expected in February?

[Index moved from 310.6 in January 1982 to 310.7 in February 1982].

As matter of simple arithmetic February figure likely to show higher 12 month increase than January figure because RPI scarcely rose at all between January and February last year.

5. Inflation rising by end year?

As we predicted, 5 per cent RPI inflation has been achieved early in 1983. Progress in recent months has been faster than was forecast at time of 1982 Budget; and may in consequence be rather slower in the months ahead. But we shall continue to experience the benefits of sound financial policies. Await Budget for new forecast, taking account all relevant factors, both helpful (eg weak commodity prices) and less helpful (lower exchange rate).

6. Effect of recent fall in sterling on rate of inflation ?

In second half of year, path of inflation may be a bit more bumpy than expected at time of Autumn Statement. But must not exaggerate possible effect of exchange rate depreciation. Suggestion of 2-3 per cent effect of recent depreciation on prices after 12-18 months much too pessimistic. Exchange rate only one factor amongst many that affect inflation, although admittedly an adverse one. Offsetting factors include weak commodity prices (including

oil), likely cuts in profit margins by exporters to UK, and Government's commitment to sound financial policies.

7. No further decline in inflation in future years?

[1983 PEWP published 1 February assumes price increases of 5 per cent in 12 months to November 1984 and 4 per cent in 12 months to November 1985.]

1983 PEWP does not contain forecasts of prices but working assumptions needed for social security programme. What actually happens will depend not least on financial policies pursued by Government which are designed to bring down inflation.

8. Inflation still not as low as competitors?

[January figures UK inflation 4.9 per cent compared 4.5 per cent in US, 3.9 per cent in West Germany, 9.6 per cent in France, 16.4 per cent in Italy and 2.0 per cent in Japan.]

UK inflation now lower than Western European (OECD Europe) average, and well below many countries - such as France and Italy. Still some way to go to match US, West Germany and Japan, but good progress being made in right direction.

9. Performance on inflation compared with main competitors no better than under previous Government?

[Jack Straw interview LBC radio 19 January.]

No. Since May 1979 annual average rate of inflation in major other Western economies no lower than during period of last Government (February 1974 to May 1979 8.5 per cent; May 1979 to December 1982 8.8 per cent). But in UK average rate of inflation under present Government well below level under previous (February 1974 to May 1979 15.4 per cent, May 1979 to December 1982 12.1 per cent).

10. TPI higher than RPI?

12 monthly increase in TPI [5.2 per cent] only 0.3 percentage points higher than for RPI [4.9 per cent] over year to January 1983.

11. Nationalised industry prices

[Increase in nationalised industry prices, water charges and London Transport fares over 12 months to January 14.1 per cent compared RPI increase of 4.9 per cent.].

Gap between nationalised industry price increases and RPI has been due in large measure to cumulative effect of years of artificial price restraint. However, NI prices expected to rise broadly in line with inflation in 1983-84. This substantial improvement is sustainable as long as the industries contain their current costs (particularly pay) in same way private sector companies must do. (See also R6).

Euro.
inflation
elsewhere

PAY

12. Implications of water industry pay settlement?

[National Water Council estimate pay settlement worth 10.4 per cent over 16 months, equivalent to 12 month settlement of 7.8 per cent].

If water industry pay settlement were widely repeated, result would be major setback to prospects for economic recovery, and thus for jobs and ultimately living standards. But no real reason for that to happen; pay settlements have on average been at considerably lower level. Important that they should continue to be kept as low as possible.

13. What is current level of settlements?

CBI data bank of manufacturing settlements shows average of about 6 per cent in round so far. But inflation is, of course, well below that level. Most settlements in the economy have yet to be concluded; important that these settlements should be kept as low as possible.

14. Economist 5 March reports pay rises average 8-10 per cent in private sector 1982-83 pay round?

[NOT FOR USE: settlements monitored by DE cover seven times as many employees as CBI databank and show 5½ per cent average rate for private sector so far this round (25 per cent of expected coverage).]

No basis for 8-10 per cent mentioned in The Economist. CBI databank of manufacturing settlements shows average of 6 per cent in round so far; individual settlements referred to in article are among highest reported in recent months.

15. What pay settlements does Government now want?

Low enough to be consistent with improved job prospects in the industry concerned. The lower the better. Certainly lower than in the past year.

16. A 3½ per cent pay policy?

The 3½ per cent pay figure [announced 1 October for calculating the pay element in public expenditure cash plans for 1983-84] does not represent a 'norm', still less an 'incomes policy'. Nor is it decision on offer to be made in any individual case. Higher or lower settlements are not ruled out. Each will be considered on merits.

Pod kissed

17. Government exhortations on pay imply aiming to cut living standards?

[Year on year average earnings growth 7.9 per cent in December compared with 5.4 per cent for RPI. Underlying earnings increase about 8¼ per cent.]

Fact that average earnings index is ahead of RPI casts doubt on wilder claims about falling living standards. But lower pay settlements are essential if we are to maintain jobs, get inflation down, and thus secure conditions for sustained improvement in living standards.

18. TUC claim that share of wages, salaries etc in national income has not changed for 25 years?

TUC figures in Economic Review 1983 show that share of income from employment (wages, salaries, employers' national insurance contributions etc) as ratio of total domestic income has been broadly unchanged since 1955. But more appropriate denominator for calculation is net domestic product, in which deduction made both for stock appreciation and 'capital consumption' - amount of nation's stock that wears out in a year. On this basis, share of income from employment has risen quite strongly.

19. Incomes Policy

Proposals for incomes policies, including recent refinements, do not avoid many of familiar problems of norms, administrative costs, and interference with market forces. Experience gives no encouragement to idea that an incomes policy can be made to work on permanent basis. They always succumb to distortions they create.

20. Public sector pensions to be adjusted to take account of overshoot?

[Compare M 1 on State pensions uprating overshoot.]

Public service pensions increases linked, by legislation, to increase in additional, earnings-related, component of State retirement pension. November 1982 increase therefore also 2.7 percentage points over increase in RPI. Therefore needs to be an adjustment to next November's increase. Decisions have yet to be taken on what that will be.

E MONETARY AND FINANCIAL POLICY

1. Monetary growth on target?

[Provisional money and banking figures for banking February to be published Thursday 8 March. Figures for banking January summarised below:

	per cent s.a.		
	M1	£M3	PSL2
January increase	1.1	0.4	0.6]

Growth rates of all three aggregates well within target range - PSL2, £M3 and M1 lie around 8½, 10½ and 11½ respectively.

2. Why did interest rates go up?

[Barclays, Lloyds and Natwest increased their base rates by 1 per cent (to 11 per cent) on 11 January and Midland theirs by ¾ per cent (to 11 per cent) on 12 January. Still down by 5 points since peak in October 1981. Long term interest rates also reduced significantly over past year.]

Structure of interest rates in domestic money markets was dislodged by fall in sterling. Interest rates in domestic money markets rose sharply in early January but have steadied. Bank base rate increases and increase in Bank of England's dealing rates reflected this. Government remain determined to maintain sound monetary conditions and to continue progress towards lower inflation. To have resisted the rise could have been interpreted as a weakening of the Government's resolve.

3. Rise in interest rates will stifle recovery (as in autumn 1981)?

Does not follow. The fall in the exchange rate, though adverse for inflation (but see also D6), will ease pressure on companies. (See also A5).

4. Prospects for resuming falls in interest rates?

Interest rates have to adjust to play their part in maintaining sound monetary conditions. Route to lower interest rates is ultimately through lower inflation.

5. Lower interest rates reduce savers' investment income?

In times of high inflation, interest rates tend to rise to compensate for this. Savers seem better off, but their capital is worth less. Partly because of Government's success in reducing inflation, interest rates have come down. Savers not necessarily affected either way. They receive less nominal interest but their capital holds its value better.

6. Will slide in sterling affect monetary conditions?

Level of sterling is one of the factors taken into account in judging monetary conditions. Recent fall in exchange rate may reflect market uncertainty about monetary conditions, though this is scarcely justified, given the reassuring position on the PSBR and monetary aggregates. Rise in interest rates reassured markets that monetary conditions required for continued control of inflation would be maintained.

7. What is position on mortgage rates?

[Mortgage rates have fallen 5 percentage points from peak in March 1982. Latest cut, to 10 per cent, came into effect for all home buyers on 1 December. Bank base rates have risen 1 per cent since then.]

At their 11 February meeting, the building societies decided not to change their rates.

8. Bank lending growing too fast?

[Bank lending starting to decrease. Increased by (seasonally adjusted) £2 billion in September, average for October and November [because of STC distortion] £1.5 billion, £0.8 billion in December and £0.6 billion in January.]

January figure lower than any last year. Bank lending to companies has steadied; fallen off markedly - perhaps reflecting companies' destocking.

9. Banks 'fixing' taxable profits?

[13 per cent drop in Barclays profits reported 7 March].

No question of banks fixing their own tax bill by manipulating bad debt provisions. Inland Revenue agree with each bank to what extent bad debts may be set off against tax, in accordance with long-standing principles. Banks' published accounts are different from private tax accounts agreed with Revenue.
[BACKGROUND: Inland Revenue wrote to British Bankers' Association on 17 January setting down principles for allowing sovereign debt to be set off against tax. These allow for reasonable flexibility].

Barclays
profits

F EXCHANGE RATE AND THE RESERVES

1. Policy towards the exchange rate/falling £?

[Since October, sterling has fallen 14 per cent in effective terms, 11 per cent against the dollar, 15 per cent against the D-Mark, 22 per cent against the yen. Sterling's low against dollar was $1.5105 on 2 February in New York. Sterling's 79.7 closing effective on Tuesday 22 February was a 4½-year low.

	October average	2 Mar low points	4 Mar noon	% change Oct -4 Mar
$/£	1.6977	1.4975	1.5136	-10.8
DM/£	4.2932	3.6450	3.6629	-14.7
Y/£	460.12	356.76	357.89	-22.2
£ effective	92.5	79.5	79.8	-13.7

Since mid-November pound has suffered repeated bouts of downward pressure. This reflected variety of causes but principal underlying factor has been fall in oil price, which will benefit oil importing countries, like Japan and Germany, more than UK.]

Government has no target for exchange rate. Nor do recent events suggest conditions exist in which pursuing a target would be a viable policy. Bank of England do intervene to seek to moderate excessive fluctuations and maintain orderly markets so far as is feasible. Government not indifferent to UK exchange rate, which is important for economy. It is one of factors taken into account in interpreting domestic monetary conditions and taking decisions on policy.

2. No change in Bank intervention level? Purchase of forward sterling, not reflected in reserves figures?

[Underlying change in reserves in February, reported 2 March, less than half January fall.]

Not our practice to comment on Bank's intervention tactics. Underlying change in reserves result of variety of transactions both debits and credits; should not be taken as indicator of market invention during the month.

3. Will lower oil prices mean further fall in sterling?

Recent slide in value of sterling in part reflected expectations that oil prices were about to fall; much of reductions announced in last few weeks have therefore been taken into account by exchange markets. On domestic front, no sound reason for rate to fall. Underlying financial position strong: Government spending and borrowing under control and on target; Government deficit, as percentage of GDP, one of smallest in industrial countries; substantial current account surplus - larger in 1982 than £3½ billion forecast only last

Stering

November; inflation falling, and fell faster over last year than in any other major country; monetary growth within targets, and signs are that it will stay there.

[For USE IF NECESSARY (eg if sterling comes under pressure): of course, if further instability in oil market, may lead to greater foreign exchange market instability.]

4. Impact of fall in sterling on inflation?

Will no doubt be some modest impact on inflation from recent fall. But probably less or slower to come through than many commentators suggest. Importers into UK have had healthy profit margins. They absorbed much of effect of sterling's fall in 1981 and they may remain reluctant to raise prices in today's market conditions. Food prices reflect 'green pound' (which is fixed separately) and has been unchanged. Commodity prices (including oil prices - one of reasons for sterling's fall) are weak - and tend to be set in dollars, where fall in sterling has been least. And, of course, some of fall could prove to be temporary.

5. Should not Government welcome fall in pound?

A lower exchange rate means higher costs to industry and the consumer: no-one should welcome that. Of course, recent fall in pound may bring some relief to British firms that are facing difficult competitive pressures in home and overseas markets, particularly from Europe and the Far East - but they must contain their costs rigorously in order to retain that benefit. We cannot solve our basic problems of competitiveness by depreciation, and no-one should doubt our determination to adhere to our counter-inflation policies. Sound money remains at heart of Government's economic strategy.

6. Improve UK competitiveness directly by encouraging exchange rate down further?

Substantial fall in exchange rate, as advocated by Opposition, would give only very temporary gains of competitiveness for UK industry. Would raise costs of imports directly and, by alleviating competitive pressures, permit general increase in prices of domestically produced goods. This would have repercussions for wage bargaining and hence trigger a general rise in costs, undermining initial competitiveness gains. We in UK have seen striking examples of this process: improvement in competitiveness following 1967 devaluation had largely been eroded by 1972; furthermore, although exchange rate fell by 25 per cent between 1973 and 1976, competitiveness was on balance unchanged. (See also A5, G10)

7. Situation has been made worse by abolition of exchange controls?

Opposition spokesmen seem to forget the lesson they surely should have learnt in 1967 and 1976. All our experience is that exchange controls have little effect in the face of strong market movements. They did not control leads and lags in trade payments, nor the

movement of massive funds invested in sterling by non-residents. (To attempt to control either would cause unacceptable disruption in trade and commercial relations).

8. Join EMS exchange rate mechanism (ERM)?

Recent events scarcely suggest that conditions that have led successive Governments to delay sterling's full membership of the ERM are yet right for us to join. Sterling as a major internationally traded currency is still being affected by oil and other factors in a different way from the D mark. Membership of the ERM is a constraint, not a policy: it carries an obligation to take action to try to defend a particular rate.

9. When will Jurgenson Report on intervention be published? What does it say?

[Recent newspaper articles eg The Times 11 February have disclosed details of the Report's conclusions eg that intervention can work, but do not expect publication before Williamsburg Summit.]

No decision yet taken about timing of Report's publication. Obviously cannot comment on it before then except to say has been useful exercise and exchange of views.

10. Progress in reduction of overseas debt?

Total official external debt now stands at around \$12 billion, compared \$22 billion when Government took office. Our remaining debt is now smaller in relation to our imports than at any time since Second World War.

G BALANCE OF PAYMENTS

[NB 1982 Q4 balance of payments to be published Wednesday, 9 March (see also 2 below) February trade figures will be published Thursday 24 March.]

1. January trade figures

[January current account deficit of £261 million, compared December surplus of £738 million. Current account surplus in 3 months to January over £1 billion, with visible and projected invisibles surplus both over £ ½ billion.]

Trade figures erratic month to month. Over last three months, current account over £1 billion in surplus; export volumes up 2½ per cent (last three months on year earlier), while import volumes rose just ½ per cent. Latest CBI Enquiry confirms recent strengthening in order books. Rise in imports in January concentrated on intermediate and basic goods; consistent with upturn in output.

2. Trade figures and current account in 1982

[Latest available published figures show 1982 current account surplus of £4.7 billion compared £3.5 billion in November IAF. (Revised 1982 current account figures to be published with Q4 balance of payments Press Notice Wednesday 4 March). Oil trade in substantial surplus (£4.6 billion); non-oil trade remains in (£2.4 billion) deficit. Invisibles in (projected) healthy (£2.5 billion) surplus. Reflects better than expected performance in Q4].

Current account surplus for 1982 - on latest available figures - £4½ billion (compared £6 billion in 1981). Achieved without £0.6 billion EC refund which will now come in 1983. Figures for late 1982 reflect mainly the continuing improvement in our oil trade. January figures notwithstanding non-oil exports have also been holding up well at a time when world trade has probably declined. Similarly, imports remained flat despite a surge in retail spending in last three months.

3. Trade in manufactures close to deficit last year ?

[Guardian report 18 February claims balance of trade in manufactured goods in 1982 fell to only £255 million.]

Press reports alleging very small surplus on manufactures in 1982 are confusing the two bases of measuring imports and exports (overseas trade statistics and balance of payments basis). When exports and imports put on comparable (balance of payments) basis, we recorded a surplus on trade in manufactures of over £2½ billion in 1982.
[NOT FOR USE: Figures underlying IAF suggest that trade in manufactures may go into deficit this year].

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4. Current account 1983 - OECD/IMF forecasts?

[IMF forecasts £2.6 billion, OECD £3.6 billion surplus in 1983, compared zero balance in November IAF - which did not allow for deferral of £0.6 billion EC rebate into 1983.]

Forecast in Autumn Statement of zero current account balance in 1983 did not allow for deferral of £600 million EC rebate into 1983. Even taking into account January figures, current account performance over last 12 months better than expected - mainly because of trade in oil. Revised forecast will be published at time of Budget. [NOT FOR USE: although current account surplus in 1983 does seem likely, it is unlikely to be on scale of 1982 surplus. Treasury forecasters believe substantial fall from recent levels is strong probability in near future.]

5. Export trends - recent

January 1983 saw continuation of very erratic month-to-month movements in exports during 1982. Export levels low last summer, particularly August, recovered since. Underlying level of non-oil exports has probably not changed significantly over past year. Good performance when, because of world recession, world trade has probably fallen (1982 first year-on-year fall since 1975).

6. Export trends last few years?

Growth in UK exports of manufactures significantly below world trade growth over 1977 to early 1981, when competitiveness worsening. With improvement in competitiveness, our share appears to have stabilised.

7. Import trends

Despite January figures, there appears to have been little change in underlying level of manufacturing imports since end-1981. Manufacturing output fell back a little in 1982, so there has probably been some continued growth in import penetration, although not at anything like same rate as in 1981.

8. Effect of lower oil prices on UK trade?

Oil only relatively modest proportion of UK overseas trade. Benefits from boost to world trade will offset (relatively small) trade balance impact.

9. Competitiveness?

See A5.

10. Non price competitiveness

Government has stressed need to improve design and quality, to meet delivery dates, and improve after-sales service. Such factors cannot be easily measured but are at least as

important as cost competitiveness. Thus for example West Germany's cost competitiveness deteriorated 20 per cent between 1970 and 1980 but she maintained here 20 per cent share of main manufacturing countries' exports. Japan managed to increase her share over this period from 12 to over 15 per cent despite slight deterioration in cost competitiveness. UK industry equally capable of non-cost improvements - witness, for example, Jaguar cars: their drive for higher quality secured them an increase in overseas sales in 1982 of 56 per cent over previous year.

11. Buy British?

See P11.

12. Protectionism?

Concerned at the extent of unfair trading practices and the damaging effect of very high tariffs and quotas in some other countries. Pressing for positive European Community action to remedy this. But will be continuing to defend the open trading system: which is in the interest of all trading nations.

13. Export subsidies?

In UK's interest to support multilateral efforts to limit use of subsidised credits which distort normal patterns of commercial trading. Until these succeed, it is our policy to provide necessary level of support for UK exporters - though of course always scope for questioning amount of subsidy worth paying to win a particular contract.

14. Selective import controls would assist economic reconstruction and reduce unemployment?

[TUC 1983 Economic Review.]

No. Looking for expansion of world trade not contraction. Protectionist measures only lead to retaliation by other countries. UK economy particularly vulnerable; one third of our output is exported. We cannot afford to have other countries putting up barriers against our trade and services. And protectionism reduces competition, which raises prices and limits choice for consumers.

15. What can UK do to safeguard our producers against dumping of subsidised imports?

UK has right to take selective action where British producers subjected to unfair competition. Under international agreements, EC and GATT can counter by imposing specific duties with aim of getting countries responsible to abandon such practices.

Competitiveness

16. Japan

Japan recently agreed Community-wide export restraints in number of sensitive product areas. Earlier announcements included package of tariff cuts, a review of standard procedures and other improvements to non-tariff barriers to trade. We welcome these developments, but we shall continue to press - bilaterally and through EC Commission - for measures to increase level of our exports to Japan, and for a more equal trading relationship.

17. Continuing capital outflow shows folly of abolishing exchange controls?

Wrong to talk about money flowing out of the country. Those who wish to invest abroad have to buy foreign currency and find someone else who wishes to invest in Britain to purchase sterling in return. The nation's net capital outflow or inflow - as a matter of arithmetic - matches the current account balance. Just as countries with deficits have to borrow abroad, those with surpluses acquire net overseas assets.

18. Portfolio outflow higher than last year?

True that there is little sign yet of end to expected period of stock adjustment following ending of exchange controls. But misleading to say portfolio investment abroad is rising. Figures for last two years seem to indicate that the flow peaked early in 1982.

19. Overseas investment takes jobs away from UK?

30 per cent of UK exports are bought by overseas firms connected with UK companies. By increasing links between UK and overseas companies, overseas investment helps UK exports and production, so producing more jobs. If UK does not take profitable opportunities to invest overseas, others will.

H FISCAL POLICY AND THE PSBR

[CGBR (February) figures to be published Wednesday 9 March].

1. Progress on fiscal policy?

[Aim is to achieve reduction in PSBR as percentage of GDP over run of years, so as to achieve lower inflation and interest rates.]

Have made progress. Government has succeeded in reducing PSBR as percentage of GDP; further reduction is projected. Inflation has fallen fast - expected to fall further (see D1). Base rates have risen but still well below (5 per cent) peak in 1981. Benefits seen in recovery of debenture market. [IF PRESSED: Would like to see rates lower still, so long as not likely to endanger progress on inflation.]

2. OECD critical of UK fiscal stance?

[Recent report on UK calls for prudent fiscal relaxation aimed at cutting costs; gives figures on cyclically-adjusted fiscal deficit (see H13).]

OECD recognise need for controlled and prudent fiscal strategy and applaud our success in reducing inflation. We have strong reservations about OECD use of cyclically adjusted Budget deficits in isolation to assess overall stance of UK fiscal policy; do not accept this has been 'over-restrictive'.

3. Balanced Budget?

[Times leader 10 February, F Williams article 23 February, S Brittan in FT 28 February.]

Government aims to reduce PSBR as share of money GDP over medium term. Illustrative profile in 1982 MTFS shows figure of 2 per cent in 1984-85. Nothing has been said about later years.

4. Recent rises in interest rates make nonsense of Government's claim that PSBR matters?

Never said relationship between interest rates and PSBR simple or direct. Certainly does not operate month to month. Basic principle - lower PSBR over run of years implies lower interest rates - still holds true.

5. How does UK fiscal stance compare with other countries?

[IMF Annual Report noted that among major industrial countries by far the largest 'restrictive shift' over past two years, equivalent to more than 3½ per cent, was that of UK.]

Many countries reducing borrowing; UK budget deficit now well below average of OECD countries. France demonstrates problems with reflation option and US experience shows that fiscal and monetary policy must be broadly consistent.

6. PSBR in December quarter

[PSBR in December quarter £3.1 billion (£2.5 billion seasonally adjusted). PSBR April-December £7.6 billion (£5.3 billion seasonally adjusted.)]

Wrong to prorate £5.3 billion to arrive at likely PSBR for 1982-83. On balance, however, December quarter figures indicate PSBR likely to undershoot IAF figure of £9 billion.

7. PSBR likely to be £8 billion in 1982-83 compared £9 billion in IAF?

It is possible. But must remember that margins of error in any precise forecast substantial.

8. What would undershoot be if Government had not taken recent measures?

[CONFIDENTIAL NOT FOR USE: At time measures taken they were thought likely to 'boost' PSBR by around £1¼ billion in 1982-83 - an estimate itself liable to quite a large margin of error.]

Rather strange question. Given the uncertainty over PSBR outturn this year it is impossible to answer.

9. EC refunds - implications for PSBR in 1982-83?

No reason at present to suggest EC refunds due to UK will not be paid over by end March 1983.

[CONFIDENTIAL NOT FOR USE: EC Commission has recently opened a new account with the Paymaster General into which has deposited funds equivalent to our refunds entitlement. These deposits are classified as miscellaneous capital receipts, and so PSBR has already been reduced. In unlikely event EC withdrew the deposits before end March, PSBR would be increased. (See also Section N.)]

10. CGBR outturn to end-January 1983? Implications for 1982-83 PSBR?

[CGBR outturn in January minus £1.8 billion, April to January £8.7 billion.]

CGBR in January minus £1.8 billion. PSBR likely to undershoot IAF figure of £9 billion. Await Financial Statement and Budget Report for latest estimate of PSBR in 1982-83.

11. PSBR persistently undershooting: Government misleading the public?

[PSBR undershot in 1981-82 by £1¾ billion and looks like undershooting again in 1982-83. It overshot in 1979-80 (by £1.6 billion) and 1980-81 (by £4.7 billion).]

Forecasting the PSBR is difficult but the errors do tend to average out over time. If, as seems likely, the PSBR undershoots this year, there will have been two undershoots and two overshoots whilst the Government has been in office.

12. Government intentions for 1983-84 PSBR?

[Autumn Statement PSBR for 1983-84 assumed to be £8 billion - 2¾ per cent of GDP; 1982 MTFS was £8½ billion. Press speculation that £2 billion available for tax cuts.].

PSBR figures in Industry Act forecast illustrative, not targets. Final decisions about PSBR and tax cuts planned for 1983-84 will be made at Budget time, not before.

13. Cyclically adjusted PSBR better guide to policy?

Government fiscal policy has taken account of recession. Acid test is level of interest rates at which PSBR can be financed, not value at some hypothetical cyclically adjusted level of output.

14. Inflation-adjusted or 'real' PSBR in surplus - isn't fiscal policy too tight?

['Real' PSBR subtracts from actual PSBR erosion by inflation of real value of Government debt. Calculations by Bank of England and others produce a surplus 'real' PSBR in most years since the 60's.]

No. Fall in inflation has raised the 'real' PSBR (because the 'inflation tax' is reduced). Real PSBR is interesting indicator but poor guide to setting policy e.g. suggests raising PSBR when inflation accelerates.

J TAXATION

1. Burden of taxation

[Total taxation (including NIC) as proportion of GDP was 34½ per cent in 1978-79 and is forecast to be 39¾ per cent in 1982-83. Corresponding figures excluding NIC are 28½ per cent and 33 per cent].

Burden has inevitably risen because of upward pressures on public expenditure caused by the recession. Increases in taxation are better - and more honest - means of financing this than borrowing, because borrowing has adverse effects on interest rates and inflation. But a higher tax burden does not necessarily mean that people are worse off, because gross earnings have risen faster than prices since 1978-79. On average, all types of household in work at all earnings levels are better off in 1982-83 than in 1978-79. [NB: individuals may have done better or worse than average.]

2. Burden of taxation risen most for the poor?

Proportion of income paid in income tax and NICs has fallen in 1982-83 for lowest paid taxpayers. Low paid with children have also benefited from generous increases in benefits such as FIS.

3. Previous reductions in personal taxation favour the rich?

1979 Budget cut absurdly high top rates of income tax to EC levels, as part of package which also involved reduction in basic rate to 30p and substantial increase in thresholds. Such action was essential to restore incentives. No 'pot of gold' in higher rate tax; restoration of 83 per cent top rate would finance a cut of under ½p in the basic rate.

4. British tax burden high by international standards?

Not so. Accurate comparisons difficult, but UK burden is about average for OECD countries [provisional 1981 data from OECD's Revenue Statistics 1965-81]. Similarly, UK taxes on personal income and UK employees' social security contributions are about average for EC countries and lower than USA [1980 provisional OECD data].

5. Cuts in taxation in 1983 Budget?

Must wait until Budget Day. Cannot comment now on size of PSBR, fiscal adjustment or individual tax changes.

6. Future of married man's personal allowance?

[Labour Party commitment to phase out in favour of increased CB etc; SDP proposals to abolish as part of proposals in document 'Attacking Poverty'.]

Government launched debate with 1980 Green Paper on Taxation of Husband and Wife.

Green Paper set out number of different options; these being considered in light of very wide range of views received. Abolition would affect many millions of taxpayers, and by itself, leave a basic rate taxpayer £5 a week worse off. For some people it would worsen poverty and unemployment traps.

7. Government unconcerned about poverty and unemployment traps

Government is concerned about poverty and unemployment traps, in context of incentives as a whole. Traps arise from attempts of successive Governments to alleviate poverty while keeping costs in bounds. Alternatives are to give less support for poor and unemployed or to let costs rip. Necessary step in right direction is to reduce burden of income tax by restraining public expenditure; long-term solution is increased real earnings resulting from sustained improvement in productivity and economic performance.

8. Taxation of Civil Service Allowances

The allowances are taxable in law. Taxing them when paid to civil servants merely ensures that private sector employees and civil servants are treated equally. It is proposed the value of the allowances be grossed up by departments so that those receiving them are not worse off as result of taxation (this also happens in outside world). But having a further look at this practice.

9. Keith Committee Report on Enforcement Powers of Revenue Departments

Chancellor has recently received first part of report. Second part should be ready later this year. Very grateful to Lord Keith and his colleagues for their work. Part I will be published 23 March. Very substantial document which deserves careful study and full consultation; this will inevitably be lengthy process.

10. Progress of working party on 'freeports'?

[Report published 3 March.]

Working party did not identify any tariff benefits which could be offered to traders in freeports that not already available under existing arrangements; but recognised marketing and presentational advantages. Recommended that two or three freeports be set up on experimental basis. [No recommendation on timing or location.] Government considering these recommendations.

11. Banks 'fixing' taxable profits.?

See E9.

K PUBLIC EXPENDITURE AND FINANCE

PUBLIC EXPENDITURE WHITE PAPER 1983 (Cmnd 8789)

[1983 PEWP published 1 February showed total spending held within previous plans:-

	1983-84	1984-85	£ billion 1985-86
PEWP 1982 adjusted for 1982 Budget changes	120.7	127.6	
Figures in Autumn Statement November 1982	120.1		
PEWP 1983	119.6	126.4	132.3

TSSC Report on PEWP published 3 March. Debate Wednesday 9 March.]

1. Government not very successful in constraining public spending?

Rate of increase in spending slowed; in 1978-79 went up 15.8 per cent, in 1982-83 8 per cent. In three years time increase over previous year planned to be 4.7 per cent. Actual ratio of public spending to GDP now falling: 44½ per cent in 1981-82, 44 (estimated) 1982-83, 43½ per cent (planned) in 1983-84 (see also A2).

2. After allowing for unexpected high fall in inflation, hasn't there been an upward revision in planned expenditure since last Budget?

Public expenditure is now planned in cash, not the 'real terms' favoured by the TCSC. In cash terms, plans for future expenditure has been substantially reduced (by £1.1 billion in 1983-84 and by £1.2 billion in 1984-85) compared with earlier plans. It is true, of course, that the Government's success in reducing rate of inflation means that cash available will go further.

3. Comparison of 1983-84 planning totals in cost terms with 1982 Budget?

[1983-84 planning total expressed in cost terms in Table 1.14 of 1983 PEWP some £1.5 billion more than corresponding figure at time of 1982 Budget (£104.4 billion, base year 1981-82), because downward revision of cash plans for 1983-84 has been more than offset by reduction in expected inflation in 1982-83 and 1983-84 since 1982 Budget.]

Expenditure plans for 1983-84 have not increased. Plans are in cash and have been revised downwards. Cost terms figures are merely derived arithmetically from the cash figures. Thus comparison of PEWP 1983 and 1982 Budget figures tells more about revision in the deflator than about revision of cash plans. In simple terms, it means that if you reduce the rate of inflation, one of the benefits is that you can buy more with the cash made available.

4. Cost terms figures for 1983-84 plans show rise compared with 1982-83 plans?

No. Comparing like with like, planning total for 1983-84 expressed in cost terms shows reduction of about ¾ per cent compared with 1982-83 plans also in cost terms (calculated using current GDP deflators). (NB. In White Paper Table 14 planning total expressed in cost terms for 1983-84 shows increase over 1982-83 of some ¾ per cent. But this comparison must be treated with caution because compares 1983-84 plans with 1982-83 outturn - caveat applicable to individual programmes as well as planning total.)

5. Growth in expenditure in 1983-84 concealed by offsetting increases in programmes with reductions in Contingency Reserve?

Provisional reserves for future years are intended to cover necessary additions to programmes, plus the operational contingency reserve for each year, offset by an element for future underspending (as explained paragraph 27 of 1983 PEWP). Reserve for 1983-84 was originally £4 billion. Of this £2.5 billion was transferred to programmes in 1982 Survey; £1.5 billion has been retained as operational reserve for year 1983-84. Transfer from reserve to programmes is in accord with intended use of reserve and does not add to planned total of public expenditure.

6. Capital spending 1983-84 compared 1982-83?

[Criticism in P&D's Market Review (February) and elsewhere that Government not providing more for spending on construction.]

Immediate problem not making nore funds available but getting local authorities and nationalised industries spend capital provision available to them. Reduction is planned expenditure compared, compared last year's plans, reflects fact that those plans were not realised. Government has taken the necessary corrective action. (See also K16-17 and R 5.)

7. Shortfall 1983-84 and later years?

[1983-84 planning total allows for net shortfall of £1.2 billion, or 1 per cent of total.]

1983-84 provision considerably smaller than 1982-83 estimated shortfall - on outturn of some £1¾ billion. This reflects both smaller Contingency Reserve and Government's plans to combat capital underspending. Shortfall for later years not directly estimated, but allowed for in 'provisional reserves'.

8. Contingency Reserve of £1½ billion for 1983-84 too small? (as suggested by TCSC)

Contingency Reserve 1983-84 is set at £1.5 billion compared with £2.4 billion in 1982-83 and £2.5 billion in 1981-82. In retrospect clear that size of the Reserve was set too high in last two years. There was substantial spare capacity in 1981-82 and is likely to be spare

capacity again in 1982-83. Size of Reserve will be reviewed at time of Budget before set finally as control total for the year.

9. Spending as much out of control when undershoots as when over-shoots?

Not out of control. Major factor in £1.7 billion in 1982-83 was that Contingency Reserve, set at £2.4 billion, was larger than needed. Other than Contingency Reserve, too early to identify other areas affected by shortfall. However, Government very concerned about local authorities' recent history of capital underspending. (See K 14-15).

10. Pay assumption for 1983-84?

Plans include sufficient cash in 1983-84 to provide for average increases in wages and salaries bills of 3½ per cent, from due settlement dates for armed forces, the civil service and certain other groups. Provision made for health service is consistent with settlements now reached covering both this year and next.

11. Price assumptions?

With exception of social security and the provision for pay for 1983-84 there are no explicit price assumptions underlying the plans. Of course, in determining the cash plans Ministers have had in mind a broad view, consistent with their general strategy, about the future course of prices. Not in general necessary for these to be formulated in precisely quantified terms, nor has it been.

12. On what price forecasts are cost terms figures for 1984-85 and 1985-86 given in TC[illegible]'s Report (Table 1) based?

Select Committee derived 1984-85 and 1985-86 figures by using 'illustrative assumptions' for social security programme plans, given in Cmnd 8789-1 (paragraph 9): GDP deflator is only available up to 1983-84. Assumptions made about movements in GDP deflator in later yars are very uncertain and figures have no more significance than the assumptions used. They have no planning significance.

13. Size of the fiscal adjustment?

Await Budget.

"Cost terms"

14. What about public spending in the longer term?

1983 PEWP only covers next three years. Risk that present t[illegible] decade could lead to significant increase in public expenditur[illegible] Government wants.

15. Contracting out of services threat to welfare state?

Aim of contracting out to improve efficiency and get the taxpayer better value for money. This will enable Government to provide better service for same cost. Nothing to do with threatening Welfare State; just sound management - irresponsible ignore any way of improving effectiveness of public services.

LOCAL GOVERNMENT

16. LA capital underspending in 1982-83

Following underspend of £¾ billion in 1981-82, local authorities seem set to underspend their capital cash limits for 1982-83 by between £1 and £1½ billion (GB figures). Some steps in hand to reduce the underspend: PM wrote last autumn to local authority associations; local authorities can apply for extra allocations (about £250 million issued so far), and can spend without limit on improvement grants; extra £150 million made available to Housing Corporation.

17. LA capital spending plans for 1983-84

[Criticism in P&D Market Review February, including comments on revenue, including debt service implications of spending.]

Plans for LA capital as a whole allow net spending one third higher than likely outturn in 1982-83. Steps taken to reduce further underspending: new rules on receipts, LAs can spend above allocations on improvement grants. Concern about revenue implications should not inhibit full use of allocations: plans for relevant LA current expenditure allow for financing costs of full planned capital programmes; many capital projects have no immediate running costs eg roads, reclamation of derelict land; others will reduce running costs by rationalisation. Government cannot guarantee there will be no underspending - LAs take the decisions. But Government will be monitoring closely, and will take further action, if needed, to encourage full use of provisions.

18. RSG settlements 1983-84

Realistic and generous: expenditure provision effectively 10 per cent higher than in last settlement and grant 3 per cent higher than 1982-83 settlement - provided authorities do not overspend.

19. Grant penalties 1983-84

Hope won't be necessary to have any. But authorities were warned in July 1982 of expenditure guidance now issued and have had ample time to adjust 1983-84 budgets to avoid incurring grant penalties.

20. Rate increases in 1983-84?

On average there should be no need for rate increases in 1983-84. If authorities spend in line with expenditure targets any increases should be low; some councils have already announced intention to reduce rates. Where rate increases are high because of overspending it will be LA's own fault.

21. Higher council house rents?

In Government's view, LAs should not need to increase rents in real terms in 1983-84. For them to decide. Government decision is about provision for housing subsidy - Environment Secretary will be consulting LA associations on basis of figure of 85p per week per dwelling. If that figure confirmed, will be possible to provide for real increase in capital investment in housing in 1983-84.

22. Green Paper on Domestic Rating System: Government response?

Carefully considering representations. Need scheme that will remedy shortcomings of present rating system and command widespread support. Taking account of pleas from industry, business, etc. (See also P7.)

FALKLANDS EXPENDITURE

23. What has defending Falklands cost us so far and what is foreseeable cost in future?

Latest assessment of costs of operation, of replacing equipment lost during conflict, and of garrison, in 1982-83 is about £750 million. Provision has been made for £624 million in 1983-84, £684 million in 1984-85 and £552 million in 1985-86 (total some £2.6 billion), on top of provision for NATO three per cent per year real growth.

24. What will be costs of repairing damage and reconstructing the Islands' economy?

Too soon to say. Work has begun on restoration of essential services. About £10 million now expected to be spent in 1982-83; further £5 million in 1983-84. Ministers have agreed on package of measures for long term development of the Islands, tentatively estimated to cost in all £31 million over next 6 years.

25. Cost of paying compensation for war damage?

Too soon to say. Expected that bulk of claims for civilian compensation will be settled in 1982-83, and remainder in 1983-84, but no accurate figure as claims still being processed. Total expected to be in region of £3½-4 million.

MR ST JOHN STEVAS' BILL

[Now going through Committee stage.]

26. Government attitude?

We recognised in our White Paper on the Role of the Comptroller and Auditor General (Cmnd 8323 of July 1981) the desirability of legislation on this subject. House ~~will~~ now ha~~ve~~s opportunity to modernise the 1866 and 1921 Acts, and that is welcome. However, there are strong arguments against the proposal in the Bill to give C & AG access to books of nationalised industries. The industries should be set clear financial targets and then be subject to minimum of interference. Bill is a move in opposite direction. All of these issues should be considered by the House.

L. CIVIL SERVICE STAFFING AND PAY

[Adjournment Debate 11 February Hansard cols 1304-10.]

1. Civil service too big/does too much/is over staffed?

Since Government came to office, Civil Service has been reduced by 11 per cent to 652,500 (at 1 January 1983). Results from reduction in functions, privatisation and improvements in efficiency. On course to achieve the 630,000 target by April 1984. This is 102,000 fewer staff in post than in April 1979, and will mean smallest Civil Service since end of Second World war.

2. Government seeking further cuts through privatisation?

[Guardian article 14 February 'Unions fight "sale of Civil Service"].

Civil Service Unions say that Government services and establishments are being 'privatised' to meet arbitrary manpower targets, and that more than a third of fall in Civil Service numbers by 1984 will be accounted for by privatisation or 'hiving-off'. Government does not accept that the 630,000 target is arbitrary; privatisation and hiving off will only account for about 12 per cent of total manpower savings. Government is reviewing need for staff in Departments over period 1984-88. This is normal good management practice. No decisions have been taken. Departments have been asked to look at scope for further privatisation and contracting out.

3. Civil service efficiency?

[TCSC published 17 January memorandum by Council of Civil Service Unions commenting on Government's reply (Cmnd 8616) to TCSC's report 'Efficiency and Effectiveness in the Civil Service').

Main theme of Council's memorandum is that drive for efficiency, motivated largely by Government's determination to reduce size of civil service, has taken no account of effects of cuts, specifically reduced quality of service. Government do not accept that reductions in manpower have been pursued regardless of effects on efficiency and effectiveness. Great savings already made with little effect on provision of services.

4. What is Government doing to improve standard of financial management in civil service?

In May 1982 launched financial management initiative aimed at promoting in each Department an organisational system in which managers at all levels have clear view of their objectives, and means to assess performance against them; well-defined responsibility for making best use of their resources; and the information, training and access to expert advice to exercise responsibilities effectively. Departments were required to submit programmes of work to Treasury and MPO by January 1983; these now being assessed by

Treasury and MPO officials. Government is committed to publish a central report on the initiative by July 1983.

5. Civil service pay negotiations in 1983?

Government have told civil service unions that there will be room for genuine negotiations and that they intend to conduct those negotiations with the view of reaching an agreed settlement. Negotiations have now started.

6. Contents of unions' claim?

[Proposals are (a) flat rate increase of £12 per week for all non-industrial Civil Servants on National Salaries up to and including £6264 pa; and (b) above this level, 'substantial' percentage increases, providing, in particular, 10 per cent on salaries up to £9758 pa. Additionally, unions propose minimum wage - for all staff aged 18 or over - of £85 per week, and reduction in working week to 35 hours net.]

Such a claim if conceded in full, would cost taxpayer about £700 million a year and add over 16 per cent to wage bill -and this in a situation where civil service generally is having little or no difficulty in recruiting and retaining staff at all levels. At second negotiating meeting (28 February) official side said they did not believe claim for reduced working hours stood up to examination; pay claim was based on generalised indices which were rarely appropriate means for decision-taking on pay. Official side wished to expand the scope of negotiation to include such matters as London Weighting and possibility of rationalising more pay scales.

7. Megaw Report

Unions have been told Government prepared to enter into negotiations with them with view to agreeing an ordered pay determination system based on recommendations of Megaw report. Unions have now confirmed their willingness to enter into joint discussion - first procedural meeting was held 22 January.

8. 'Adjustment' and public sector pensions?

See D 20.

9. Taxation of civil service allowances

See J8.

M SOCIAL SECURITY

[Benefits uprated by 11 per cent 22 November 1982 which included 9 per cent to take account of inflation. RPI increase in 12 months to November was 6.3 per cent, hence 9 per cent was 2.7 percentage points more than needed to preserve value of benefits. Announced in Autumn Statement that November 1983 uprating would be adjusted to have regard to this over-provision for inflation. Chief Secretary made clear to Social Services Committee on 15 December, however, that saving would be £180 million in 1983-84 - less than would be achieved by full recovery of overshoot.]

1. Pensions should not be adjusted next November?

Pensioners better off this year by extent of overshoot. Only question how much of this real increase continues beyond November 1983. No decisions on precise rise in pensions can be taken until nearer Budget time - Government will then have to take account of priorities inside and outside social security programme. But it will not go back on its pledge to maintain real value of pensions over lifetime of this Parliament.

2. Public expenditure saving?

Full recovery of overshoot would save about £250 million in 1983-84; about £800 million in a full year. But social security programme has been reduced by £180 million in 1983-84 by £500 million in 1984-85 and £600 million in 1985-86. This reflects Government's judgment of appropriate level of expenditure. Exact level of November 1983 uprating will be settled at Budget time, when Government will, as usual, take wide range of factors into account.

3. Improve benefits by using difference between planned adjustment and full savings?

There is constant pressure from both sides of House for whole variety of improvements. Government will have to determine priorities, eg between change in individual benefits and adjustment in next uprating. Decisions will, as usual, be taken at Budget time.

4. Government said in 1981 it did not intend to seek powers to provide for automatic recovery of overshoot?

[Minister of State Social Services on Social Security Bill 2nd Reading 24.2.81: 'if it was our intention to ask the House for a right to have a clawback in perpetuity - the exercise of that power year by year - we should have included such a power in the Bill. We have not done so.']

Decision we have taken is to make an adjustment of the programme. Decisions on the uprating will be taken at Budget time. True that legislation would be required in certain circumstances. Too early to speculate on the form of that legislation.

5. Labour pledges to pensioners?

[Labour pension proposals 'revealed' to pensioners' delegation 1 March. Include raising single/married pension to third/half average earnings, reducing pension age to 60, increasing

Pensioner x
Labor

death grant to £200, doubling Christmas bonus. Little new in proposals, most of which published in 'Labour's Programme 1982'.]

Cost of implementing pensions proposals in full probably over £12 billion in fully year. No proposals given for raising this money: but cost could be met by eg raising basic tax rate from 30p to 42p in £ or doubling employee's NIC to 18 per cent.

6. Government should restore abatement of unemployment benefit?

[Amongst recommendations of Social Services Committee Report on Autumn Statement, published 29 January.]

Social Services Secretary made Government position clear in debate on 22 November. Government do not regard abatement of unemployment benefit as permanent measure; are considering question of its restoration in light of available resources and other decisions on uprating of benefits.

7. Government may act on company pensions?

[FT articles 21-22 February suggest Treasury document contains 'well advanced' proposals to give employees right to choose between company pensions schemes and individual pension provision, to encourage job mobility and employee interest in pension schemes.]

Government's position on occupational pension schemes clearly stated by Social Services Secretary in House on 19 October. Early leavers not fairly treated at present. In interests of equity and job mobility, Government looks for voluntary remedial action by pension schemes. Far preferable to compulsion which would impose extra costs on employers. Government does, however, accept in principle need for legislation on disclosure of information by schemes to members (to help latter ensure schemes managed in their best interests).

8. War Widows?

Government have impressive record of provision for war widows. As promised in Manifesto, have exempted war widows' pensions from income tax and given pensions to widows of 'other ranks' who left forces before 1950. War widows' pensions fully protected against inflation during this Parliament.

N EUROPEAN COMMUNITY

1. UK budget settlement for 1982

[European Parliament on 16 December rejected draft supplementary and amending budget established by Council of Ministers on 8 November to make the necessary budgetary provision for our refund payments. This action obstructed implementation of settlement reached by Foreign Ministers 26 October, providing for basic gross refund of around £630 million (about £480 million net) by end-December.]

Council of Ministers established new draft supplementary budget for 1983 on 1 February and European Parliament adopted it 10 February. Payments of 90 per cent of our refunds can now be expected to follow.

2. Refunds for 1983 and later

Commission communication of 17 November provided in UK view a suitable framework for discussion within the Community of Budget problem; hope that progress will now be made quickly. PM has said will have to be discussed at next European Council on 21-22 March if solution not found by then. On 7 February, Chancellor gave Press Conference in Brussels at which emphasised importance of finding lasting, fair and comprehensive solution to problem of budgetary imbalances. He offered some ideas to show possibilities.

3. UK objectives for longer-term negotiations?

Government has made it clear that, in spite of our relative economic position, UK is prepared to remain a net contributor - but only on a very modest scale.

0. Will Government withhold contributions?

We very much hope the issue of our Budget contributions can be satisfactorily settled without need for recourse to such a step.

5. Commission Green Paper on 'own resources' system: Commission in financial crisis?

Commission's Green Paper on 'own resources' was published 7 February. We are studying this carefully. Our opposition to an increase in the 1 per cent VAT ceiling is well known. With proper control of CAP spending we believe Community should have sufficient resources, even after enlargement.

6. Policy for CAP reform

Key measures are price restraint, curbs on surplus production and strict control of the growth of guarantee expenditure.

7. Costs of CAP to UK consumers

The Minister of Agriculture has dealt with a number of questions on this. Costs to consumers of the CAP as such depend on nature of alternative support system that is envisaged. Arrangements leading to a reduction in the cost of food to the consumer could well involve increased costs to taxpayers.

8. European Monetary System exchange rate mechanism

See F8.

P INDUSTRY

1. Latest statistics of output and investment?

See Section B and Commentary at end of Brief.

2. Companies' financial position?

[NB company sector borrowing in 1982 Q3 includes large element of unidentified transactions (-£1 billion)

£bn

	1979 Year	1980 Year	1981 H1	H2	1982 H1	Q3
Net borrowing requirement (+)/repayments (-)	+6.1	+6.5	-1.7	+6.2	+6.0	+1.9
Financial surplus (+)/deficit (-)	-2.9	-1.4	+1.3	+0.7	-1.1	+0.8]

Financial position of industrial and commercial companies (excluding North Sea) improved in 1981, relative to 1979 and 1980. Some apparent deterioration in borrowing requirement second half 1981 due to slowdown in de-stocking and unwinding of delays in tax payments because of the civil service dispute. Figures for first three quarters 1982 suggest companies' borrowing requirements remain high, but much less so than in 1979 or 1980; encouraging figure for Q3 financial surplus - though this may principally reflect a further round of improvement - in part reflected companies' efforts to cut costs, for example by de-stocking.

3. ICCs liquidity ratios in 1982 Q3?

[D. Industry's survey of 200 large companies (published 4 March in British Business) shows some improvement in liquidity between 1982 Q3 and Q4. Total current assets rose by over £¾ billion, while current liabilities fell marginally (seasonally adjusted). Current liquidity ratios rose from 73 per cent to 79 per cent for manufacturing companies only.]

Latest D Industry figures show encouraging improvement in liquidity, particularly for manufacturing, between 1982 Q3 and Q4. (Over 1982 as whole, total current assets of companies surveyed increased, but this was more than offset by the rise in total current liabilities resulting in fall in liquidity ratio.) Although liquidity ratio for manufacturing companies surveyed is still lower than in 1981 Q4, it has improved considerably since 1980.

4. Profits/rate of return still too low?

[Gross trading profits of industrial and commercial companies (ICCs) (net of stock appreciation) rose 17 per cent 1982 Q3 compared 1981 Q3 but increase was from a very low

Compared

base. ICC's real pre-tax rate of return (except North Sea was just over 3 per cent in 1981, and only 2 per cent in manufacturing - half previous cyclical low figure in 1975.]

Government can help best by getting inflation down and setting sound basis for sustained recovery. Fundamental improvement in ICC's rates of return depend on better performance by companies. Some encouragement from recent productivity gains and trend towards moderate pay settlements.

5. Real rates of return on capital lower in UK than elsewhere?

[OECD statistics comparing US, Japan, France and UK show net rates of return to fixed capital in non-financial corporations in 1976-80 lowest in UK - though all on a downward trend. 1980 figures: US 13 per cent, Japan 15 per cent, France 9 per cent, UK 5 per cent.]

Figures show how policies of earlier administrations have allowed profitability to slide in UK. Sound basis for sustained recovery rests on reducing inflation, increased productivity gains, and moderation in pay settlements which creates conditions for better performance by companies.

6. High interest rates damaging for industry and investment?

Banks' base rates still 5 percentage points lower than October 1981. Outside analysis suggests that a 1 per cent reduction in interest rates improves the net financial position of the company sector by about £250 million over a full year.

7. Lower rates for industry?

De-rating one of a number of possible ways of assisting industry and business, but in last Budget preference given to other forms of relief, notably reductions in NIS. De-rating would be expensive, though less so if applied to industry alone - even so, 10 per cent de-rating would cost about £140 million per annum. Legislation would be required.

8. Government believes levels of industrial support are far too high? Intend to trim?

[Press reports of internal Whitehall paper, questioning value of some forms of aid.]

Public spending is too high generally, and industry support no exception. This is not to say that industrial support is not useful in a period of transition; but must aim at deploying a declining total more flexibly, focussing help where really needed and on industries and technologies of tomorrow.

9. Government review of regional policy?

[Parliamentary Answer 14 February Hansard col 13].

Officials of the Departments concerned have been reviewing the effectiveness of the main instruments of regional policy. Now for Government to consider whether to commission

further work in particular areas that would be necessary to prepare for any changes. Have not yet reached conclusions on any aspect. Too soon to say when will reach conclusions.

10. What kind of industrial base and pattern of employment is Government aiming for?

Size and shape of industry and employment are not determined by Government but primarily by the action of market forces and competition. Government does not prepare detailed sectoral forecasts of industrial output and employment. Not true that Government indifferent - or hostile - to traditional manufacturing industry.

11. Buying British

Many British products have always been competitive. New competitive ones coming onto market. When buying British must take account of price or quality - otherwise would only render firms incapable of competing internationally. But should give British products - and ourselves - a full and fair chance.

12. Government help for small firms

Last Budget provided further help for small businesses, increasing the number of measures taken so far from which small firms can benefit to nearly 100. Enterprise package included further reduction in weight of corporation tax; further increases in VAT registration limits; increases in global amount available for loans under Loan Guarantee Scheme (see below); and doubling of investment limit under Business Start-Up Scheme to £20,000 a year. These measures designed to encourage start-ups and existing firms.

13. Response to Loan Guarantee Scheme?

[8,300 guarantees already issued - about half to new businesses. Total lending under scheme over £275 million. Budget provided for lending ceiling in first year (to May 1982) to be raised from £100 million to £150 million and for further £150 million to be available in second year (to May 1983). Thirty financial institutions now participating. Speculation in FT 28 February that future of scheme will be announced as part of Budget].

Scheme operating successfully. Too early to assess overall cost. First year cost covered by premium income. Now clear that payments will exceed income in this financial year. By end-January 1983, payments under scheme in respect of 'called' guarantees exceeded premium income plus recoveries by £3.8 million. Outcome of review will be announced shortly.

14. Enterprise zones

Response to first eleven zones has been encouraging; many new firms have been set up and others expanded. (But too early to assess overall success). Proposed sites for nine new zones in England announced by Environment Secretary 15 November; sites for two new zones for Scotland, one for Northern Ireland and one for Wales have also been announced. One more for Wales under consideration.

R PUBLIC OWNERSHIP AND PRIVATISATION

NATIONALISED INDUSTRIES - GENERAL

1. EFLs for 1982-83

Estimated outturn for external financing in 1982-83 published in PEWP 1983 is £2.3 billion - about £½ billion down from 1982 PEWP. British Telecom expected to undershoot its EFL substantially, BSC to overshoot substantially.

2. EFLs for 1983-84?

Nationalised industries EFLs for 1983-84 were announced in Autumn Statement; EFLs revised to allow for NIS reductions were announced 23 December. No further revisions included in 1983 PEWP. Overall, external finance in line with previous plans. £2.6 billion being made available to nationalised industries in 1983-84.

3. What is Government doing to improve nationalised industries' efficiency?

We continue to press for greater efficiency within NIs. We are setting realistic financial targets and performance aims. Rolling programme of Monopolies and Mergers Commission investigations has been set up. Introduction of market forces provides the greatest incentive to efficiency.

INVESTMENT

4. Step up nationalised industries' investment to/improve infrastructure/provide orders to private sector/ boost economy?

Government has not prevented the industries from carrying forward a large number of profitable investment programmes. Wasteful to provide funds for public sector projects with lower returns than those in private sector. Unfortunately, pre-tax rate of return on nationalised industries' capital (including subsidies) in 1981 (latest available figure) was minus ½ per cent, compared with 3 per cent for industrial and commercial companies.

5. Continuing undershoot on investment plans?

No Government can unconditionally guarantee a particular level of nationalised industries investment. Events outside industries' control may cause investment plans to be revised downwards. Industries substantially undershot investment plans in 1981-82, and look like doing similarly in 1982-83. Even so, actual investment this year expected increase about 14 per cent over 1981-82 levels (allowing for privatisation, changes in BT's treatment of certain investment, and excluding BNOC and BTDB). PM has encouraged industries to fulfil

their investment plans. If they do, investment in 1983-84 should increase by about 12 per cent over this year's estimated outturn (excluding BNOC).

PAY AND PRICES

6. Nationalised industries' prices

Gap between nationalised industry price increases and RPI has been due in large measure to cumulative effect of years of artificial price restraint. World oil price rises of 1979 and 1980 have also played an important part. We greatly regret the need for these increases, but holding prices down artificially would distort market forces and add to burden on taxpayer. Differential between NI prices (including water charges and London Transport fares) and RPI now (January 1983) about 9 per cent, compared with 14 per cent in January 1981; over half of present differential explained by LT fares and last winter's electricity rebate. NI prices expected to rise broadly in line with inflation in 1983-84. This substantial improvement is sustainable only so long as the industries contain their current costs (particularly pay) in the way that private sector companies have to do.

7. UK industrial energy prices above those of European counterparts?

Energy and Industry Secretaries had discussions with industry about energy prices on 17 February. CBI's recent report on comparative energy prices confirms that vast majority of gas and electricity consumers pay comparable prices to their European competitors. Some disparities exist for limited number of intensive users of electricity. But measures worth over £300 million in energy cost savings introduced in last two Budgets to help industry. And, on average, electricity prices will not increase in 1983 (see R8). Cannot expect disparities to be closed entirely especially where due to different costs of supply. Sole way of reducing real electricity costs is by containing costs of generating industry.

8. Prospects for gas and electricity prices in 1983?

Freeze on industrial gas prices to be extended to first nine months of this year. Domestic gas prices expected to rise by no more than rate of inflation. On average, industrial and electricity prices will not be increased at all in 1983. These decisions taken by the industries themselves purely on commercial grounds.

PRIVATISATION

9. Special asset sales in 1982-83?

Estimated outturn for 1982-83 around £550 million. Full details of this year's receipts will be published after end of financial year. Sale of Britoil completed and will amount to about £625 million, paid partly in 1982-83 and partly in 1983-84. ABP has been sold, producing net

receipts of £46 million. Wytch Farm disposal is still proceeding [IF PRESSED: but is unlikely to be completed this financial year.]

10. What further sales expected?

Sale of British Gas Corporation's major offshore oil assets expected in 1983-84. Aim to sell shares in British Telecom after General Election and to transfer British Airways to the private sector as soon as possible.

11. What sales included in special asset sale targets for future years?

[PEWP 1983 has targets of £750 million (previously published target £600 million) in 1983-84, £1500 million (previously £600 million) in 1984-85 and £500 million in 1985-86, for proceeds from special sales of assets.]

Not practice to disclose details of composition of targets because timing of sales dependent on market conditions and price information commercially sensitive. changes from 1982 PEWP reflect decisions on privatisation since last targets published, and make allowance for additional disposals likely to arise from continuing scrutiny of potential candidates for privatisation.

12. Marketing of public assets - Amersham/ABP and Britoil failures in different ways?

[Heavy oversubscription for British Aerospace, Cable and Wireless, Amersham International, Associated British Ports, followed by large increases in prices when shares first traded; about 75 per cent of Britoil shares left with subunderwriters and large discount when first traded].

No. These companies successfully privatised. Pricing issues not easy especially when company's shares have not previously been traded. In addition, cannot accurately anticipate movements in market after price fixing but while offer still open.

13. Contribution to giving people satisfaction of property ownership?

Exercise of returning enterprises from State ownership to ownership by the public has included measures to promote employee share ownership in the enterprise they work for; for example free offers of shares (British Aerospace, Cable and Wireless, Amersham, Britoil, ABP); preference in allocation of shares (B Ae, C & W, Amersham, Britoil, BP, ABP); provision for matching shares - one for each share subscribed for - (B Ae, Amersham, Britoil, BP, ABP). Most radical initiative taken by consortium of managers and employees who bought National Freight Company. Inclusion of small shareholders' bonus in Britoil sale designed to reward small investors who retain an interest in the company.

S NORTH SEA AND UK ECONOMY

1. Current discussions among OPEC oil Ministers/OPEC fear UK will 'undercut'?

OPEC Oil Ministers in touch with each other about a new production programme. UK will not be joining OPEC. Our interests are not identical with those of the OPEC countries, since oil does not provide a major proportion of our exports or of Government revenues.

2. Latest published forecast of North Sea revenues?

[Autumn Statement (Industry Act forecast) projections (in money of the day) of Government revenues from North Sea: £6½ billion in 1981-82, £7 billion in 1982-83, £7½ billion in 1983-84. Higher than 1982 FSBR projections, partly because of higher production, partly higher oil prices. P&D as reported in The Times 4 January assess Government revenue will peak in 1983-84. Aberdeen University computer runs 'see sharp falls' The Times 31 January.]

Must remember that oil revenue projections are crucially dependent on inherently uncertain cost, price and production assumptions. Prospects for North Sea tax receipts in 1983-84 improved since 1982 FSBR and Autumn Statement because of higher than assumed sterling oil prices and production. Recent $3-3.5/b reduction in North Sea oil prices offset by fall in exchange rate. In general, higher estimates by others are based on combination of higher expected future production and prices and lower expected future capital expenditure.

3. Impact of lower oil prices on UK?

Lower oil price, on balance, good for UK. Large disruptive movements in any direction are in no one's interest. But modest and gradual fall would reduce inflation and boost growth - both good for us. Trade balance effect relatively modest, and fall in $/£ rate since autumn enough to offset effect on revenues of recent proposed fall in BNOC oil prices.

4. Reduction in North Sea oil prices?

[On Friday 18 February BNOC announced $3/b - $3.50/b reduction in North Sea oil prices backdated to 1 February, taking price of Forties crude to $30.50/b.]

North Sea oil prices matter for BNOC. In interests of market stability BNOC sought for some time to resist a price reduction. It has now responded to market changes which have already taken place. It is not leading the market. US, USSR, Egypt and Ecuador have reduced prices officially. Many producers have reduced prices covertly.

5. Will BNOC's price reduction 'stick'?

Price negotiations a matter for BNOC's judgement. Demand for North Sea oil will obviously depend on pricing policy of other producers. BNOC will continue to monitor market developments, and act accordingly.

6. Government to relax North Sea fiscal regime?

Oil companies have argued for substantial reductions in taxation. No decisions have been taken. But fact-finding discussions have been taking place with UKOOA and individual companies since the summer to try to close the gap between Government's and companies' assessment of North Sea taxable capacity. These discussions will soon be concluded.

7. Onerous tax system damaging future field developments?

[Energy Select Committee report published 27 January on depletion policy claims North Sea tax regime inhibiting development. Recommends overhaul of tax regime].

Will obviously study report carefully. But remember that other adverse factors - falling oil prices earlier this year; high development costs - much more important than tax. Detailed study has shown that, under current tax structure, levels of profitability should still be sufficient to make exploration and development attractive. Hope that this structure will provide more secure and stable tax regime. A completely new regime would not necessarily be more stable. Certainly disruptive in short term. Aberdeen University study shows UK taxation on marginal fields to be one of world's 'more lenient'.

8. Taxation of petrochemical feedstocks

[Government has announced that new rules on valuation of ethane for petrochemical use in interaffiliate transfers (Finance Act Section 134) should be extended to mixed streams of gas with a large ethane component. ICI complain that the extension and the rules themselves give unfair advantage to their integrated oil company competitors and have taken out writ against the Government.]

Government convinced that new formula will give fair valuation. New valuation will not have effect of providing subsidy to ICI's competitors. Have done best to reassure ICI. Will resist ICI's legal action.

9. Benefits of North Sea should be used to strengthen economy?

[Contribution of North Sea to GNP estimated at 4 per cent of GNP in 1981. Not projected to rise significantly before 1985.]

Yes. Government's strategy derives greatest possible long-term benefit from North Sea. Revenues ease task of controlling public borrowing. This will help to achieve lower level of interest rates to benefit of industry and economy as a whole. Without North Sea revenue other taxes would be higher or public expenditure lower. But keep revenues in perspective. Less than 6 per cent of total General Government receipts in 1982-83.

10. Are we really any better off for North Sea oil?

We are better off with oil - at current oil prices - than we would have been without it. We have been spared fall in real national income that other industrial countries have suffered

following oil price rises. But North Sea oil costly to produce, so we are not necessarily any better off than we would have been had oil prices not risen. No need therefore for possession of oil to require a contraction in our industrial base.

11. 'Precipitous drop' in North Sea output after 1985?

[Phillips & Drew forecast of oil output almost halving between 1985 and 1990 - FT 4 January.]

Hazardous to forecast so far ahead. But always known that oil output would peak in mid-1980's and then decline - though not as steeply as P&D expect. Cannot be complacent about effects of falling North Sea output. Best thing we can do is pursue our present economic policies so that economy in better shape when output begins to decline.

T WORLD ECONOMIC DEVELOPMENTS AND INTERNATIONAL FINANCE

1. World recovery under way?

[Article The Times 3 February quotes number of examples in Europe and US where leading indicators have begun to turn around, suggesting world on brink of recovery.]

Welcome early but still tentative signs that are beginning to emerge of the recovery in prospect. Now that inflation and interest rates have been brought down, forecasts point to recovery in output for the industrial countries of around 1-2 per cent this year. Progress on inflation should ensure recovery is soundly based and sustainable.

2. Why don't low inflation countries increase demand?

Lower inflation and interest rates provide basis for recovery partly by reducing costs of public expenditure and providing room, within counter-inflationary fiscal and monetary objectives, for greater real growth of activity. Deliberately expanding demand would only rekindle inflationary expectations and jeopardise successes from which real and sustainable growth of demand already being created.

3. IMF quota/GAB increases: international Keynesianism?

[M Beenstock FT 2 March accuses Chancellor of being monetarist at home and Keynesian abroad because, he argues, larger quotas will swell world liquidity].

Increases in IMF resources are necessary contingency measure in present circumstances. IMF has vital role in helping economies to adjust while lessening risk of excessive disruptions which could damage both individual economies and international system. Important also to note that use of resources will be spread over number of years and will be accompanied by firm adjustment programmes.

4. Next steps?

Important for IMF members to seek necessary parliamentary authority soon, so that growth increase can be made effective by beginning of 1984. [IF PRESSED Chancellor will be seeking early approval for increase in UK quota and GAB contribution].

5. What about a fresh allocation of Special Drawing Rights? Why not allocate SDRs exclusively to LDC's?

IMF will be examining desirability of further SDR allocation, in light of current trends in growth, inflation, and international liquidity. We have an open mind about case for further allocation. The case for allocating SDRs exclusively to LDCs may, as on previous occasions,

form part of this review. Allocating SDRs in this way would require amendment of the Fund's Articles.

6. Prospects for US economy?

[Some hopeful signs that US economy has begun to recover, including increase in industrial production, rising volume of housing starts and sharp rise in index of leading indicators. Mr Feldstein, Chairman of Council of Economic Advisers, has said that Administration will revise up forecast of growth (of 1.4 per cent in 1983 over 1982).

Welcome early but still tentative signs of recovery in US.

7. US Budget

[US Administration forecasts budget deficits ranging from $207 billion in current FY to $300 billion in FY 1988 if no action taken. Administration has proposed package of measures aimed at reducing deficit, including freeze on Federal expenditure, structural reform of social security system and $45 billion cuts in defence expenditure. These would reduce budget deficit to $189 billion in FY 1984 and $117 billion in FY 1988.]

Share Administration's concern over potential size of budget deficit. Glad to see Administration's proposals to reduce public sector deficit over medium term. In line with UK's fiscal policy as set out in MTFS. Vital for world recovery that Administation and Congress can agree quickly on firm measures to reduce deficit if US interest rates are not to rise again, as economy recovers.

8. US monetary policy

[In his semi-annual testimony to Congress, Federal Reserve Chairman Volcker announced following monetary targets for 1983 (1982 target in brackets) - M1 4-8 per cent (2½-5½), M2 2-10 per cent (6-9), M3 6½-9½ per cent (6½-9½); and M2 base changed to average February - March 1983 level. M2 growth surged in January but as base is still unknown, remains to be seen how tight monetary conditions will be this year.]

Chairman Volcker has stressed US administration remains committed to reducing inflation. Glad to see, therefore, US authorities acting flexibly within firm overall stance of monetary policy.

9. Anti-inflation policies are working

[Consumer price inflation down from a year ago in all 7 major economies on latest available figures: US (from 8.9 to 3.9 per cent), UK (12.0 to 4.9 per cent), Japan (4.7 to 1.8 per cent), Italy (17.3 to 16.4 per cent), Canada (11.4 to 8.3 per cent) France (14.0 to 9.7 per cent), Germany (6.4 to 3.9 per cent) NB US authorities modifying consumer price index to give less weight tomortgage costs: this may result in higher figure for inflation over past year.]

UK performance in bringing down inflation in past year as good as any, and better than most of our major trading partners. Falls in inflation together with falls in interest rates offer better prospects for recovery this year.

COMMENTARY ON RECENT ECONOMIC DEVELOPMENTS AND STATISTICS
7 MARCH 1983

Summary comment

The effective exchange rate has fallen nearly 14 per cent since October. Interest rates have risen 2 points since end November. However, the direction and the consistency of policy are unchanged. Gentle upward trend in GDP(O) during 1982 and some signs that output is picking up both inside and outside manufacturing sector. RPI inflation below 5 per cent in January (and Government forecast comfortably achieved); but inflation path later this year may be a little bumpier than previously expected. New Government forecast with Budget on Tuesday, 15 March. Outside forecasters expect UK GDP growth of around 1½-2 per cent this year.

World Economy: expectations held by most forecasters for an upturn in activity of 1 per cent last year unfulfilled. A modest recovery in world trade is expected this year.

- U.S. economy is showing increasing, but still tentative, signs of recovery; leading economic indicators rose by unusual 3.6 per cent in January; highest increase in more than 3 decades; President's chief economist now speaking of 5 per cent year-on-year growth for fourth quarter of 1983;

- world commodity prices are at their lowest level in real terms for thirty years;

- oil prices are weak and likely to remain so for the near future; North Sea prices proposed to fall by $3 per barrel to $30.50;

- consumer price inflation (OECD major 7) 5½ per cent in January ranging from 16 per cent in Italy to 4 per cent in Germany and 2 per cent in Japan on latest figures;

- average world 3-month interest rates around 9½ per cent at 28 February over 5½ points fall between February 1983 and Q3 1981; US 3 month rate about 8½ per cent on 28 February; U.S. prime rates out ½ point to 10½ per cent on 21 February real interest rates remain clearly positive;

- EMS currency realignment expected by the market in the near future;

. world trade volume (weighted by UK markets) fell by some 2-3 per cent in 1982;

. total industrial production for the OECD Major 7 fell 4¼ per cent in the twelve months to December; in the US it rose in January but still 3 per cent lower than a year before;

. unemployment (OECD total) 8.9 per cent in December compared with 6.7 per cent for average 1981 on standard definitions.

UK Balance of Payments: non-oil trade balance has deteriorated quite sharply but current account remarked in stronger surplus during 1982 than forecast in IAF. Both the loss of competitiveness during 1979 and 1980 and a smaller world market are affecting our non-oil trade but the volume of exports held up well in 1982 and are unlikely to fall below their 1981 levels. Too much attention should not be focused on sharp deterioration in current account in January 1983; surplus still £1.2 bn in 3 months to January.

. OPEC and Third World countries are cutting back on imports because of low commodity prices, high interest rates and debt problems in some countries.

. import volume rose sharply as activity recovered in 1981 and import penetration rose too; in 1982 non-oil import volumes showed little change on 1981 H2.

. the effective exchange rate at 79·6 on 7 March . Pound now below both 87-93 range occupied for the last year and May 1979 level (86.3).

Financial Developments

.Monetary aggregates well within target range for 1982-83, M1 and £M3 towards top of range, PSL2 towards bottom;

.most banks raised base rates by 1 point on 11 January (to reach 11 per cent) following similar increase on 26/29 November; short term interest rates down 5½ points since October 1981; base-rates down about 5 points;

.mortgage interest rates down to 10 per cent, first time since 1978;

.real interest rates remain clearly positive (as elsewhere, particularly in the US and Japan);

.CGBR £8¾ billion in 10 months to January.

.PSBR: £5.3 billion in 9 months to December; Industry Act Forecast of £9 billion in 1982-83 at upper end of range of likely outcomes.

.Underlying fall in the reserves during February was $171 million.

Inflation

.retail price inflation, 4.9 per cent in year to January.

.TPI increase in 12 months to January was 5.2 per cent;

.Wholesale price inflation: input prices up 8.0 per cent in year to February compared with 9.3 per cent in January following lower oil prices; output prices up 7.1 per cent in year to February. (Lowest 12-monthly increase since July 1973.)

GDP and industrial production

.GDP(O) rose slightly in Q4 1982 confirming gently upward trend apparent since Q1 1982. Increase of 1½ per cent since 1981 Q2 trough largely reflects increased North Sea oil production. Construction output in 1982 Q3 was 3 per cent up on previous quarter and 2 per cent higher than in 1981 Q3. Industrial output also remains broadly flat but is 1½-2 per cent above spring 1981 trough almost entirely due to increased oil and gas production; the underlying level of manufacturing output is below its trough level (1981 Q1).

Demand Components

.consumer spending held up well during the recent recession and has continued to strengthen since 1982 H1. Some fall in RPDI (see below personal sector) offset by lower savings ratio. Retail sales fell slightly in January but remain buoyant, increasing 1½ per cent in 3 months to January on preceding three months. Consumers' expenditure in Q4 1982 (provisional) 1½ per cent up on previous quarter (this is being reflected in the relative buoyancy of the consumer goods industries) and, in 1982 as a whole was 1 per cent above its 1981 level.

.gross fixed investment recovered slightly in 1982 Q3 from a disappointingly second quarter and in the first three quarters of 1982 was 3 per cent up on same period in 1981,

but 8½ per cent below its average 1979 level. Manufacturing investment (including leasing) in Q4 1982 1 per cent down on Q3 1982 and 3 per cent down between two halves of 1982. Total capital expenditure by manufacturing, distribution and service industries up 2 per cent on latter comparison.

.Manufacturers' and distributors' reduced stocks in Q4 1982 by £370 million (1975 prices) - comparable to the severe de-stocking of 1980 and 1981.

.government consumption is virtually flat. In 1982 Q3 it was 1½ per cent up on the preceding quarter and on its level in the same period last year;

.non-oil exports held up well in 1982 against a 3 per cent fall in world trading activity;

.imports rose very sharply between the two halves of 1981, reflecting both the increase in activity and increased import penetration, before stabilising but non-oil import volumes this year have shown little change since 1981 H2.

Productivity and Competitiveness

.manufacturing productivity continues to rise - at 2 per cent in year to Q4 1982. Productivity now 12½ per cent up on end 1980;

.manufacturers' unit wage/salary costs up less than 6¾ per cent in Q4 1982 on a year earlier;

.Cost competitiveness has improved around 25 per cent since early 1981, but remains around 10 per cent worse than in May 1979 (whole of this deterioration is attributable to excessive wage costs).

Company Sector

.ICCs pre-tax real rates of return on capital in 1981 were very low; only 2 per cent in the manufacturing sector. Some slight improvement likely this year.

.after falling in first quarter of 1982 gross trading profits (net of stock appreciation) of ICCs rose in the third quarter by 4¾ per cent; and in first 3 quarters of 1982 were 11½ per cent up on their average 1981 level;

·non-North Sea profits fell 4¼ per cent in Q3 1982 on previous quarter but in first three quarters of 1982 were 13¾ per cent up on their average 1981 level;

·gross profits of North Sea oil companies in the first 3 quarters of 1982 were 8 per cent up on their average 1981 level;

·ICCs financial surplus was £0.5 billion in six months to September 1982 following deficit of £0.3 billion in previous six. Over same period net borrowing requirement fell from £9.1 billion to £4.0 billion.

·working days lost through industrial stoppages estimated at 313,000 in January. Total for whole of 1982 (7.9 million) well below average of 12 million for last ten years.

·insolvencies: provisional totals for 1982 are 5.707 bankruptcies and 12,039 company liquidations, increases of 11 per cent and 40 per cent on 1981.

Personal Sector

·wage settlements in 1981-82 were on average around 7 per cent, 2 per cent lower than in the previous round;

·underlying rate of increase in average earnings in year to December 1982 was about 8¼ per cent;

·CBI reports that pay settlements in manufacturing industry averaged 6.1 per cent in 1982 Q4 compared with 6.8 per cent in the third quarter. Bulk of settlements will occur in 1983 H1;

·real earnings broadly flat in last 12 months but RPDI in the third quarter is about 2¾ per cent lower than the average for 1981.

Labour Market

·UK employed labour force fell 2.0 million (7¾ per cent) between 1979 Q2 and 1982 Q3 (heavily concentrated in manufacturing); between 1981 Q3 and 1982 Q3 the fall was 658,000; manufacturing employment fell a further 85,000 (1½ per cent) between 1982 Q4 and preceding quarter;

.employed labour force fell more in the third quarter of 1982 (200,000) than in the previous quarter (160,000);

.total registered unemployment fell by 26,000 to 3.20 million (13.7 per cent on the new basis) in February (fall reflects seasonal factors);

.UK adult unemployment rose by 18,000 to 3.00 million (12.9 per cent) in February; no clear indication of any change in underlying rate of increase. Notified vacancies increased by 2,000 to 124,000 in February but volume of vacancies remain at very low levels;

.notified redundancies rose by 8,000 in January to 71,000;

.other labour market indicators hours lost through short time working fell back slightly in December to 1.7mn, after increasing steadily since July 1982 Q1. Hours of overtime worked remain broadly flat.

Forward Indicators

.car production (seasonally adjusted) fell to 67,000 in January from 76,000 in December while commercial vehicle production fell from 22,700 to 20,800 (sa); new car registrations (not seasonally adjusted) in 1982 were about 5½ per cent up on 1981; in January 1983 was the best January on record and import penetration fell back from 60 per cent to 57 per cent. New commercial vehicle registrations rose 6 per cent between 1981 and 1982.

.steel production (seasonally adjusted) rose by 33 per cent in January and in 3 months to January the weekly rate of production rose by 1½ per cent but was 25 per cent down on same period in 1981;

.the volume of new construction orders, have shown a steadily upward trend since last spring and in 1982 Q4 was 2 per cent up on the previous quarter and 8 per cent higher than a year earlier. Engineering orders rose about 7 per cent in three months to November compared with previous three months but remain 7.8 per cent down on year earlier;

.Latest DOI investment intentions survey suggests a 3 per cent fall in manufacturing investment between 1982 and 1983 but other components of investment (distribution and services) are more encouraging;

[illegible]
[illegible]

.<u>total housing starts</u> in three months to January rose by over 13 per cent on previous 3 months, but broadly flat during 1982. Total completions in 1982 Q4 recovered slightly from their level in the middle of 1982 but in the year as a whole were about 14 per cent down on 1981;

.<u>CSO's index of longer leading indicators</u> rose to November, thereafter unchanged to January; shorter leading and coincident indicators have continued to rise over recent months.

CBI's February Trend Enquiry is encouraging: features a substantial swing in balance of firms expecting an increase in manufacturing output from -5 (January) to +8, biggest single positive swing since January 1981. Total and export order books also improved substantially. Firms do not regard themselves as overstocked as in earlier months, and this is contributing to improved outlook for output. Slight increase in proportion of firms expecting to raise average domestic selling prices is nevertheless low by historical standards.

<u>Outside forecasts</u>

.<u>Outside forecasting groups</u> - for 1983 consensus of outside forecasts around 1½-2 per cent, assuming some recovery in world economy, with inflation forecast around the 6-7 per cent range by the end of 1983 in many assessments.

<u>New Government Forecast</u> to be published with Budget on Tuesday, March 15.

<u>Key indicators to be published in week ending 11 March</u>

Tues 8	:	Monetary aggregates (Feb - provisional)
Wed 9	:	CGBR (Feb)
	:	Balance of payments (4th qtr)
Thur 10	:	Vehicle production (Feb - provisional)
Fri 11	:	Building societies' figures (Feb)
	:	Steel production (Feb)

beat, a number of important targets, viz:-

a. taking the Government Actuary's assumption of earnings growth of 6½ per cent between 1982-83 and 1983-84, it reduces or matches average rates of tax and NIC for 1982-83 for all people who are contracted-in;

b. it reduces average rates of tax compared to 1978-79 for married men on at least three quarters of average earnings - ie two thirds of married men; and

c. because I have rounded up the married man's allowance, it gives all married men a tax reduction of just over £2 a week.

4. As I told you, there is a huge choice of figures on which to base alternative calculations. They are all complicated by two things: the increases in NIC which we have had to make (including this year's special addition to the contracted out rate): a total of [ ] per cent for those contracted in, and of [ ]per cent for those contracted out; and the very large increase in average earnings that has taken place.

5. With this in mind one can make a variety of comparisons with 1978/79, Labour's last year. A reduction in the average percentage rate of tax and NIC combined so the levels in that year would require an increase of more than 30 per cent over indexation. On average rates of tax alone, indexation plus 8½ per cent improves the position for most married men, but indexation plus 15 per cent would be needed to match 1978/79 for a majority of the single (and earning wives).

6. The figure of indexation plus 10 per cent (which I mentioned) would, as it happens, restore allowances to their 1978/79 level as

a percentage of earnings. But it would take no particular tricks, since that milestone is seldom mentioned. Reference is more often made to the real value of the allowances ~~exhorted~~ expressed (as "Rooker-Wise" requires) in terms of prices; and by that yardstick indexation plus 3 per cent is sufficient to restore the 1978/79 level. (I see that the ITN Budget Factbook, for example, suggests that to "provide complete indexation during /his/ time as Chancellor" would require me to make an overall increase this year of 12 per cent and we shall be doing better than that.) Average earnings, of course, have have ~~done much better~~ increased more than prices still - which means that all the options, including bare indexation, show real net earnings in 1983/84 after tax and NIC as higher than in 1978/79.

measured

7. There is one other thing which may have been obscured by the way in which we are obliged to do our initial arithmetic in terms of the first year net PSBR cost of any measure. The income tax cuts which I now propose cost, on that basis, "only" £1 billion. But the full year revenue cost of such income tax cuts, including indexation, is about £2.5 billion, and that is the figure which will hit the headlines.

8. I believe it would be unwise to go beyond that, not least because it would make the PSBR up to £8.5 billion. To announce an intention of borrowing more, in nominal terms and as a proportion of GDP, next year than in the current year would cause considerable surprise, since it would be inconsistent with the strategy we have been following over the years. And it would reduce still further our very limited room for manoeuvre in face of a sharp fall in oil prices.

9. So I really do think that 8½ per cent makes sense, and that more would be a mistake.

(G.H.)
8 March 1983

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Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

PRIME MINISTER

INCOME TAX THRESHOLDS

You asked me to think about the possibility of increasing the thresholds by 10 per cent.

2. In recent weeks I have, as you know, been planning a 8½ per cent increase, largely because:-

a. we need to demonstrate our determination to go on reducing borrowing, even if only at a moderate rate; this means a 1983-84 PSBR which can be shown (after some "rounding down") as no more than £8 billion;

b. which in turn means that our scope for total net tax reductions (after indexation and valorisation) is, on the latest forecast, limited - in terms of PSBR impact - to some £1.5 billion (and even that is pushing it a bit); and

c. to target more than three quarters of these reductions on individuals, rather than business and industry - and more than two thirds on the single area of income tax thresholds - would be open to sharp criticism. (Frankly, I think we would be accused of electioneering.)

3. There is no particular magic about the 8½ per cent figure: the £1 billion relief (in PSBR terms) which it represents, on top of indexation, is more important. But 8½ per cent does meet, or

/beat

beat, a number of important targets, viz:-

a. taking the Government Actuary's assumption of earnings growth of 6½ per cent between 1982-83 and 1983-84, it reduces or matches average rates of tax and NIC for 1982-83 for all people who are contracted-in;

b. it reduces average rates of tax compared to 1978-79 for married men on at least three quarters of average earnings - ie two thirds of married men; and

c. because I have rounded up the married man's allowance, it gives all married men a tax reduction of just over £2 a week.

4. As I told you, there is a huge choice of figures on which to base alternative calculations. They are all complicated by two things: the increases in NIC which we have had to make (including this year's special addition to the contracted out rate): a total of 2.5 per cent for those contracted in, and of 2.85 per cent for those contracted out; and the very large increase in average earnings that has taken place.

5. With this in mind one can make a variety of comparisons with 1978/79, Labour's last year. A reduction in the average percentage rate of tax and NIC combined to the levels in that year would require an increase of more than 30 per cent over indexation. On average rates of tax alone, indexation plus 8½ per cent improves the position for most married men, but indexation plus 15 per cent would be needed to match 1978/79 for a majority of the single (and earning wives).

6. The figure of indexation plus 10 per cent (which I mentioned) would, as it happens, restore allowances to their 1978/79 level as

/a percentage

a percentage of earnings. But it would take no particular tricks, since that milestone is seldom mentioned. Reference is more often made to the real value of the allowances expressed (as "Rooker-Wise" requires) in terms of prices; and by that yardstick indexation plus 3 per cent is sufficient to restore the 1978/79 level. (I see that the ITN Budget Factbook, for example, suggests that to "provide complete indexation during /his/ time as Chancellor" would require me to make an overall increase this year of 12 per cent and we shall be doing better than that.) Average earnings, of course, have increased more than prices - which means that all the options, including bare indexation, show real net earnings in 1983/84 after tax and NIC as higher than in 1978/79.

7. There is one other thing which may have been obscured by the way in which we are obliged to do our initial arithmetic in terms of the first year net PSBR cost of any measure. The income tax cuts which I now propose cost, on that basis, "only" £1 billion. But the full year revenue cost of such income tax cuts, including indexation, is about £2.5 billion, and that is the figure which will hit the headlines.

8. I believe it would be unwise to go beyond that, not least because it would make the PSBR up to £8.5 billion. To announce an intention of borrowing much more, in nominal terms and as a proportion of GDP, next year than in the current year would cause considerable surprise, since it would be inconsistent with the strategy we have been following over the years. And it would reduce still further our very limited room for manoeuvre in face of a sharp fall in oil prices.

9. So I really do think that 8½ per cent makes sense, and that more would be a mistake.

(G.H.)
8 March 1983