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T.R.1.

Ps/ *Secretary of State for Trade and Industry*

DEPARTMENT OF TRADE AND INDUSTRY
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4 August 1987

David Norgrove Esq
Private Secretary to the
Prime Minister
10 Downing Street
LONDON
SW1A 2AA

Dear David,

INDUSTRIAL PRODUCTION

Your letter of 14 July recorded the Prime Minister's request for a more detailed analysis of industrial output since 1979.

... The enclosed note sets out the pattern of output growth by individual manufacturing sectors since 1979, examines the main broad explanations of the differences in growth rates between industries and gives a number of examples of companies which have had a significant effect, for better or worse, on their industries.

I am copying this letter, with a copy of the paper to Tony Kuczys (HM Treasury).

Yours
Paul

PAUL STEEPLES
Private Secretary

At 1st glance, this looks innocuous enough. But it overlooks the important 'central' point I made in a recent speech. PST draft a letter to point out this omission.

JF1ANM

MANUFACTURING OUTPUT SINCE 1979

Introduction

PS/Prime Minister's letter of 14 July noted the latest encouraging industrial production figures and requested a more detailed analysis of the pattern of industrial growth since 1979. This note describes the performance of the many separate sectors comprising manufacturing industry since the first half of 1979, provides some suggestions as to why sectors have performed differently, and identifies some companies which have had a significant effect on performance.

Manufacturing Output

2 Manufacturing output in total reached a peak in the first half of 1979 - though at a level 4% below the previous 1973 peak - and then declined sharply - by nearly 16% - until the first quarter of 1981. Since then it has recovered strongly though there was a dip in output from 1985Q2 to 1986Q1. In the three months to May 1987 manufacturing output was nearly 17% higher than the 1981Q1 trough level but still 1.4% below the 1979 peak. [See Chart 1].

3 This average manufacturing performance, however, conceals widely different patterns of development within subsectors. For the purposes of this note manufacturing has been subdivided into 41 sectors [See Annex A]. Any level of disaggregation is inevitably fairly arbitary and it is quite likely that sub-sectors within the 41 selected sectors will have behaved differently from the sector itself. The 41 sector breakdown has been chosen to give a readily comprehensible summary of developments in the main industrial groups.

4 The disaggregated information on output growth for these 41 sectors is set out in Table 1. The first column of Table 1 shows the percentage change in output between the first half of 1979 and the first quarter of 1987 - the latest period for which there are reasonably good estimates at this level of disaggregation. The sectors are ranked in order of output growth which emphasises the wide

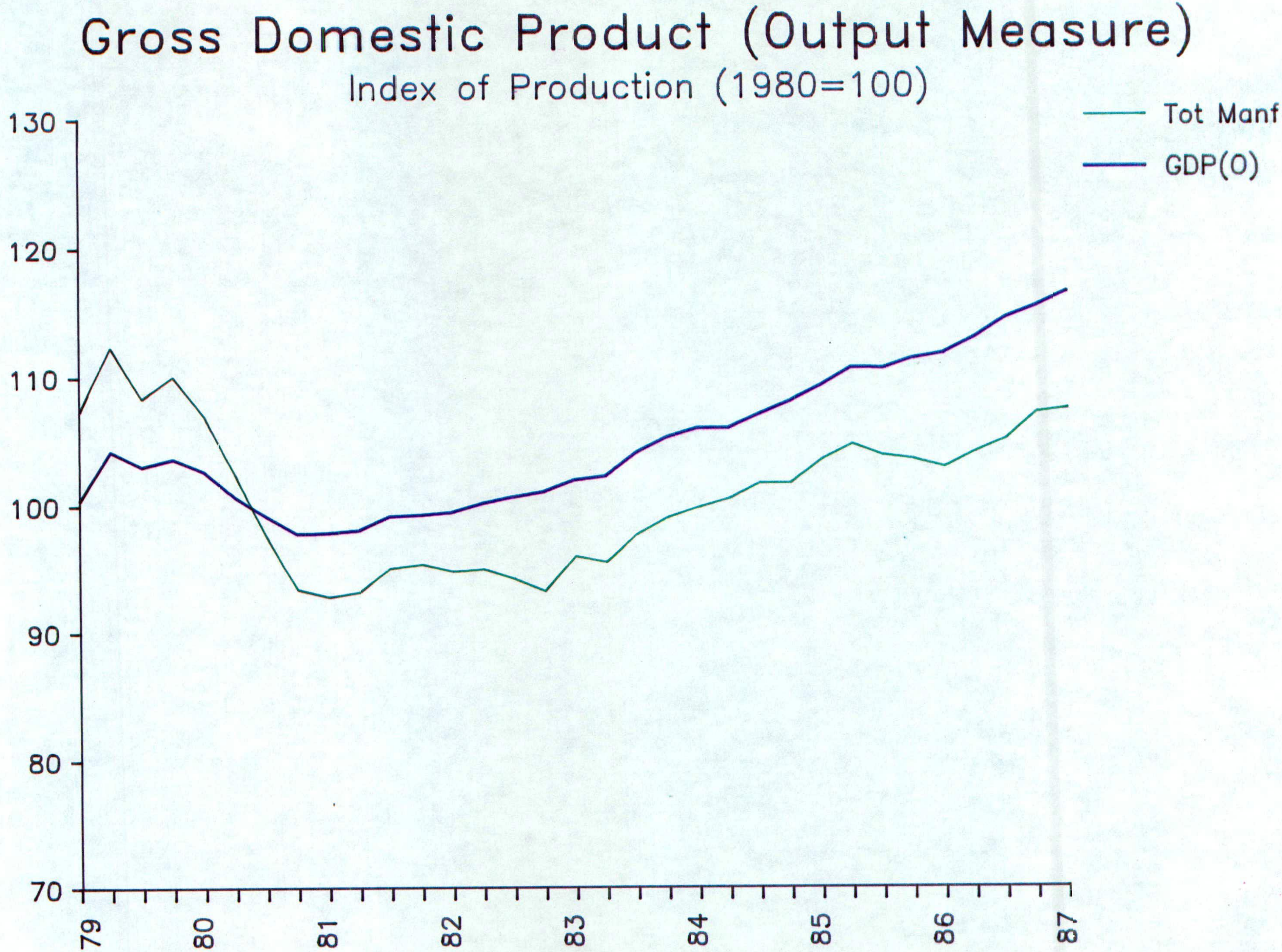

Gross Domestic Product (Output Measure)
Index of Production (1980=100)
Tot Manf
GDP(O)
130
120
110
100
90
80
70
79
80
81
82
83
84
85
86
87

TABLE 1

MANUFACTURING OUTPUT

(Seasonally adjusted/Constant Prices)

	(1987Q1)/(1979H1) (% Change)	(1987Q1)/(1981Q1) (% Change)	Weight (%)	(1987Q1)/(1979H1) Contribution to growth
	Column 1	Column 2	Column 3	Column 4
Computers and other office machinery	228.2	240.8	1.4	2.6
Electronic capital goods (inc. Telecommunications)	36.6	28.0	4.2	1.3
Electrical consumer goods	35.9	60.6	2.1	0.8
Pharmaceuticals	33.7	42.0	2.1	0.7
Aerospace	31.1	0.5	2.9	0.7
Plastic products	31.0	57.4	2.3	0.7
Consumer chemicals	24.2	33.1	1.4	0.3
Ordnance and small arms	18.5	23.4	0.6	0.1
Industrial chemicals	11.7	27.9	5.5	0.6
Instrument engineering	11.6	13.5	1.4	0.2
Food	6.8	7.8	9.1	0.6
Printing and publishing	6.3	15.2	6.1	0.4
Drink	4.6	5.0	3.3	0.1
Hand tools and finished metal goods	0.9	23.7	3.3	0.0
Clothing	- 1.3	21.0	2.3	- 0.0
Glass	- 4.0	12.3	0.9	- 0.0
Household textiles and fur	- 4.0	2.9	0.4	- 0.0
Non-Ferrous metals	- 4.0	4.8	1.5	- 0.1
Building materials	- 4.2	8.1	2.6	- 0.1
Extraction of minerals and metal ores	- 7.8	17.1	0.7	- 0.1
Heavy industrial plant	- 13.2	- 12.6	2.0	- 0.2
Timber and wooden products	- 14.3	7.6	1.5	- 0.2
Pulp, paper and board	- 15.2	1.9	3.0	- 0.5
Leather and leather goods	- 15.3	24.0	0.3	- 0.1
Ferrous metals	- 16.8	16.5	1.9	- 0.4
Furniture	- 17.1	4.9	1.6	- 0.3
Textiles	- 18.4	12.5	3.3	- 0.7
Mining, construction and associated equipment	- 18.9	3.6	1.9	- 0.4
Other machinery	- 19.5	- 0.4	8.5	- 1.7
Footwear	- 19.8	1.5	0.7	- 0.2
Electrical industrial goods	- 21.2	6.9	3.7	- 0.8
Rubber products	- 22.5	1.4	1.5	- 0.3
Tobacco	- 23.7	- 27.4	1.1	- 0.2
Ceramics abrasives and asbestos	- 28.9	- 6.5	1.1	- 0.3
Metal-working machine tools	- 31.5	- 3.0	1.4	- 0.4
Other vehicles	- 31.7	- 26.1	0.8	- 0.2
Motor vehicles and parts	- 31.7	9.5	5.7	- 2.1
Shipbuilding	- 34.2	- 29.1	1.3	- 0.5
Other manufacturing	- 34.7	- 12.0	1.0	- 0.4
Basic metal forming	- 37.9	- 6.0	2.8	- 1.3
Man-made fibres	- 56.8	- 34.1	0.3	- 0.2
Total Manufacturing	- 2.2	+ 15.9	100	- 2.2

range in fortunes experienced between sectors: at the one extreme the output of the computer and the office machinery sector grew by 228% while at the other extreme the output of the man-made fibres industry fell by over 50% between 1979H1 and 1987Q1. As manufacturing output as a whole in 1987Q1, was still 2.2% below the 1979 peak level it is not surprising that in 27 of the 41 sectors output has yet to regain the 1979H1 levels. But in sectors accounting for nearly half of total manufacturing production, output is now above the 1979 peak.

5 Comparing output levels between the first half of 1979 and the first quarter of 1987 gives little impression of how output changed within the period and in particular how output has recovered since the first quarter of 1981 - the trough for manufacturing as a whole. The charts in the Annex B plot the movements in output for each of the sectors using total manufacturing as a reference point. Column 2 in Table 1 presents the growth for each sector between 1981Q1 and 1987Q1. Over this period manufacturing output grew by nearly 16%, though in 10 of the sectors output was still below the 1981Q1 level. For industries where output is now above the 1979 level, there were strong recoveries since 1981Q1 in electrical consumer goods, plastic products, pharmaceuticals, consumer chemicals and hand tools and finished metal goods. Of the industries where output was still below the 1979 peak levels there were strong recoveries in leather goods, clothing, ferrous metals, and the extraction of minerals and metal ores. The really weak industries, those well below 1979 levels and showing little sign of recovery are heavy industrial plant, footwear, electrical industrial goods, rubber products, tobacco, ceramics, other vehicles (eg railways, motor cycles etc), shipbuilding, basic metal forming and man-made fibres.

6 Column 3 and 4 of Table 1 give some idea of what effect the different output changes shown in column 1 had on average manufacturing growth since 1979 by taking account of the relative sizes of the sectors. Column 3 shows the weight of each sector in total manufacturing in 1980 and column 4 uses this information to show how each sector contributed to the change in total manufacturing output.

The sectors contributing most to the growth of output have been computers and other office machinery, electronic capital goods, household electrical goods and plastic products. Those industries having the largest negative influence were motor vehicles, miscellaneous machinery for industry and basic metal forming.

Why has performance differed?

7 Without entering into very detailed analysis of factors underlying the performance of individual sectors (efficiency, design, management, skills, restrictive practices, etc), output in a broad sense will be determined by a combination of demand for the sector's products and its relative competitiveness compared with foreign producers. This note examines the growth in domestic demand for the products of each sector and its trade performance. It also looks at how changes in the structure of UK output compare with the experience of other industrialised countries, to see to what extent performance can be explained by common world-wide factors.

Domestic Demand

8 Although manufacturing industry exports some 30% of its output and imports meet some 35% of the home demand for manufactured goods, differing rates of growth of domestic demand for the products of industrial sectors will have an important influence on changes in their output. Unfortunately statistics directly comparable to the rate of growth of output listed in Table 1 do not exist for demand but it is possible to get a good feel for the importance of demand by looking at the growth of domestic demand at current prices between 1979H1 and 1986Q4. These are presented in column 1 of Table 2 which, for ease of comparison, uses the same ranking as Table 1.

TABLE 2

DOMESTIC DEMAND AND TRADE BALANCES

(all in current prices)

	Domestic Demand 1986Q4/1979H1 (% Change) Column 1	Ratio of Trade Balance*/ Domestic Demand: Year to 1979Q2 Column 2	Ratio of Trade Balance*/ Domestic Demand: Year to 1987Q1 Column 3	Changes in Ratio of Trade Balance/Domestic Demand (Columns 3-2) Column 4
Computers and other office machinery	257	- 17	- 21	- 4
Electronic capital goods (inc. telecommunications)	157	7	4	- 3
Electrical consumer goods	124	- 11	- 31	- 20
Pharmaceuticals	109	28	28	0
Aerospace	134	22	48	+ 26
Plastic Products	114	- 1	- 9	- 8
Consumer chemicals	114	13	3	- 10
Ordnance and small arms	84	32	39	+ 7
Industrial chemicals	53	7	11	+ 4
Instrument engineering	118	- 2	- 15	- 13
Food	67	- 13	- 12	+ 1
Printing and publishing	140	5	2	- 3
Drink	72	12	4	- 8
Hand tools and finished metal goods	74	4	- 5	- 9
Clothing	69	- 11	- 18	- 7
Glass	58	- 2	- 9	- 7
Household textiles and fur	69	- 5	- 11	- 6
Non-ferrous metals	5	- 19	- 22	- 3
Building materials	105	3	2	- 1
Extraction of minerals and and metal ores	16	- 57	- 65	- 8
Heavy industrial plant	85	23	8	- 15
Timber and wooden products	54	- 35	- 36	- 1
Pulp, paper and board	83	- 20	- 24	- 4
Leather and leather goods	47	- 14	- 16	- 2
Ferrous metals	- 19	3	1	- 2
Furniture	79	- 2	- 14	- 12
Textiles	48	- 8	- 21	- 13
Mining, construction and associated equipment	47	29	20	- 9
Other machinery	60	24	8	- 16
Footwear	73	- 22	- 35	- 13
Electrical industrial goods	71	20	9	- 11
Rubber products	39	9	0	- 9
Tobacco	58	21	22	+ 1
Ceramics, abrasives and asbestos	55	24	14	- 10
Metal working machine tools	49	0	- 9	- 9
Other vehicles	15	6	- 10	- 16
Motor vehicles and parts	80	- 4	- 26	- 22
Shipbuilding	- 14	- 8	- 24	- 16
Other manufacturing	117	1	- 15	- 16
Basic metal forming	- 3	3	0	- 3
Man-made fibres	6	13	- 1	- 14
Total Manufacturing	69	- 1	- 7	- 6

* Trade Balance = Exports - Imports

9 It is immediately apparent that there is a fairly strong correlation in the ranking between the growth of domestic demand and the growth of output. This is not surprising. It is difficult to imagine a sector growing buoyantly when domestic demand is falling rapidly. The performance of several sectors, especially shipbuilding, ferrous and non-ferrous metals, basic metal forming, man-made fibres and other vehicles, have clearly been affected adversely by structural changes in demand. Similarly some sectors, particularly computers and office machinery, electronic capital goods, electrical consumer goods, aerospace, printing and publishing, and instrument engineering, have clearly benefited from the positive structural changes in demand that have taken place.

Trade Performance

10 But in a world economy characterised by relatively free trade, buoyant domestic demand does not of course guarantee buoyant domestic output. The ability of industry to compete against overseas producers both in the UK and world markets will also be a key factor since domestic demand can be supplied by imports while buoyant exports can offset weak demand in the home market. Annex C presents the growth in exports and imports in volume terms for each of the 41 sectors. It is not easy to draw firm conclusions from these figures because industries which have shown strong export growth have in many cases also seen strong import growth, no doubt reflecting changes in the pattern of demand and the general growth of world and intra-industry trade.

11 A better way of assessing the influence of trade flows on output growth is to look at changes in the trade balances for each sector. Columns 2 and 3 of Table 2 present those trade balances (standardised for purposes of comparison by dividing by domestic demand) for the years ending 1979Q2 and 1986Q4. For output to have grown faster than domestic demand over the past seven years, the

change in the trade balance over the period (column 4 of Table 2) must be positive. Put another way, trade performance will have added to output growth over and above that resulting from domestic demand growth, only in those sectors where the change in the proportionate trade balance is positive.

12 It is clear from Table 2 that trade performance has held back the growth of output over this period in the vast majority of manufacturing industries. Only in five industries, aerospace, ordnance and small arms, industrial chemicals, food and tobacco has trade performance contributed positively to output growth. In most cases the total output of these industries also grew relatively strongly; but in the case of tobacco a strong trade performance was unable to overcome very weak domestic demand. It is interesting to note that in a number of sectors, both at the top and bottom of the output growth league table, trade performance and domestic demand have been pulling in opposite directions. Thus electrical consumer goods output has grown well, despite a very poor trade performance, because of very buoyant domestic demand. Similarly a poor trade performance by motor vehicles and parts has resulted in poor output performance despite above average growth in domestic demand.

13 The general conclusion that trade performance has, on the whole, held back output growth is not surprising in view of the very strong real exchange rate over the early part of this period and the development of the large trade deficit in manufactured goods. With the fall in the oil price, the real exchange rate is now at a level much more conducive to manufacturing industry. If real exchange rates remain around their current levels, it is likely that trade performance in the coming years will contribute much more to output growth.

<u>How do the changes in the structure of UK manufacturing compare with those experienced by other countries?</u>

14 To a considerable extent the changes in the structure of UK manufacturing over the last eight years were not unique to this country.

Other major industrial countries appear to have experienced rather similar patterns of structural change. This suggests that the reason for such changes should be sought in factors such as changing tastes and technologies, changing energy prices, and competition from newly industrialising countries which are not peculiar to the UK but which relate rather to the nature of individual industries.

15 Internationally comparable data are not available at the level of sectoral disaggregation used in this note. Nor are they available on such an up to date basis. However a recent DTI analysis compared the growth rates of 29 individual manufacturing sectors in the UK, USA, Japan, Germany and France, over the period 1979 to 1984, with that of manufacturing as a whole. Individual sectors were compared across the five countries in terms of whether they grew faster or slower than total manufacturing.

16 Compared to manufacturing as a whole, output growth in a number of UK sectors followed a path similar to other OECD countries. Examples of sectors where growth was relatively strong in most countries are electrical machinery (including industrial machinery and domestic applicances), plastic products and other chemicals (including pharmaceuticals). Sectors which tended to be universally weak were usually mature industries. In particular, leather, textiles, footwear and iron and steel declined in importance in all five countries between 1979 and 1984.

17 In some cases ouput changes in the UK did diverge from trends in other major economies though there are few instances where the UK experience differed radically. UK performance in professional goods (instrument engineering) appears relatively strong compared with that in all the other countries except Japan. Similarly, the UK was unusual in that its food products and industrial chemicals sectors showed output growth well above that for total manufacturing. UK sectors whose relative decline was not reflected to such an extent elsewhere include transport equipment and rubber products. Finally, UK structural change was unusual in that its metal products and

petroleum refineries sectors did not suffer the relative decline apparent in other countries and in the absence of growth in the paper products industry.

Examples of companies which have had a significant effect on changes in output

18 It is not possible to calculate directly the contribution of each company to the change in output of its sector because of the restrictions relating to statistical confidentiality. The examples that follow have been prepared from the DTI's regular contacts with industry and an analysis of company accounts. For the most part the companies identified are among the largest in the sector and so are likely to have had a major impact on the change in that sector's output. However, some sectors, particularly the engineering ones, are groupings of smaller heterogeneous industries where changes in output may be influenced by the performance of relatively small companies.

19 For computer manufacturing generally, there has been significant growth in production but this has mainly been by the big US and Japanese multinationals. In a fast expanding market ICL has not held its own, although recently there has been a marked increase in its profitability. In the microcomputer market Apricot has performed particularly well. Sales increased 10 fold between 1980 and 1984 and nearly doubled the following year.

20 A strong performer in the pharmaceutical sector has been Glaxo. Its sales and profits have increased steadily since 1982.

21 In aerospace the two most important companies are British Aerospace and Rolls Royce. On average their turnover has grown by 17.3% pa and 11.4% pa respectively.

22 While there are a number of successful companies in industrial and consumer chemicals the one which has had most effect on overall performance has been ICI. In 1984 ICI became the first UK company to achieve profits of over £1bn. After a slight set back in 1985 due to increased competitive pressures and a less favourable exchange rate, 1986 saw profits rise by 11% and sales volume by 7%. First quarter results for 1987 gave profits of £334m with improved margins in all sectors.

23 Within instrument engineering a number of relatively small firms have been particularly successful. The largest of these is Oxford Instruments whose products are based on superconducting technology and include superconducting magnets for magnet resonance medical diagnostic imagers. VG Instruments is another successful company which manufactures scientific instruments and equipment for semiconductor manufacturing. Both companies have received Queen's Awards for technology and exports.

24 There are a number of large companies whose poor performance has contributed to the decline of certain sectors. In motor vehicles and parts as well as the decline in production by what is now the Rover Group, production by Ford and Peugeot Talbot also fell. The performance of the merchant shipbuilding sector is dominated by British Shipbuilders and Harland and Wolff. The more than 70% reduction in output since 1979 has been the result of the fall in demand and the intense international competition, particularly from the Far East.

25 In the machinery sector the receivership of Stone Platt and the sale and subsequent break-up of the Bentley Group by Sears Holdings is reflected in the fall by 80% in the output of the textile machinery industry. Similarly in the process plant sector turnover by John Brown Engineering fell from £700m in 1982 to £500m in 1986 and in the furnace industry the largest UK company, Wellman, has seen its profits and turnover fall.

26 However even in the machinery sector there are companies which have bucked the trend. J C Bamford in the construction equipment sector more than doubled its turnover between 1979 and 1986, with profits showing a similar pattern. Other examples would be Crossfield Electronics in the printing equipment sector and APV-Baker in that sector and the food and drink processing equipment industry.

27 Courtaulds and Coats Viyella are the two major textile and clothing companies. After a bad patch in 1981 when profits fell to £5m Courtaulds turned itself round and has seen a rapid increase in profits since then. Coats Viyella is also doing well.

28 An exception to the overall decline in the production of passenger cars is Vauxhall. Its production has increased fairly steadily since 1979 and is now nearly 3 times higher than 8 years ago.

29 Between 1983 and 1985 two overseas companies: the Bridgewater Paper Company and the Shotton Paper Company have established new capacity in the paper and board industry in the UK so that now the UK is capable of producing about 36% of its annual newsprint consumption.

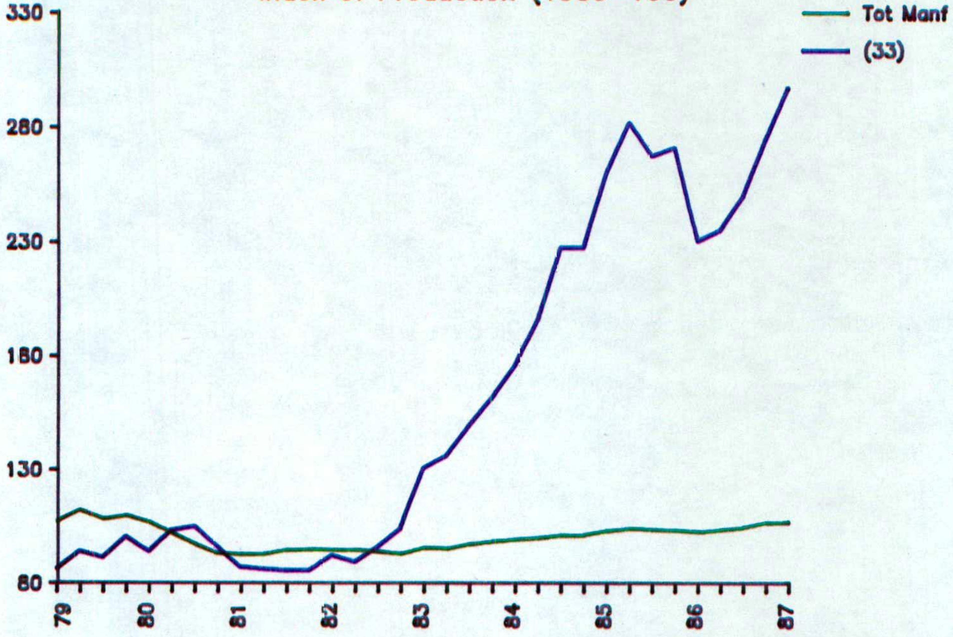
INDUSTRY GROUPINGS USED FOR DISAGGREGATED ANALYSIS

	Industry	SIC Group
1	Extraction of Minerals & Metal Ores	210, 231-239
2	Ferrous Metals	221-223
3	Non-Ferrous Metals	224
4	Building Materials	241-243 and 245
5	Ceramics, Abrasives and Asbestos	244, 246, 248
6	Glass	247
7	Industrial Chemicals	251-256
8	Pharmaceuticals	257
9	Consumer Chemicals	258-259
10	Man-Made Fibres	260
11	Basic Metal Forming	311-313
12	Hand Tools and Finished Metal Goods	314-316
13	Heavy Industrial Plant	320
14	Metal-Working Machine Tools	322
15	Mining, Construction and associated equipment	325
16	Other Machinery	321, 323- 324, 326-328
17	Ordnance and Small Arms	329
18	Computers and other office machinery	330
19	Electrical Industrial Goods	341-343
20	Electronic Capital Goods (inc. Telecommunications)	344
21	Electrical Consumer Goods	345-348
22	Motor Vehicles and Parts	351-353
23	Shipbuilding	361
24	Aerospace	364
25	Other Vehicles	362-363, 365
26	Instrument Engineering	371-374
27	Food	411-423
28	Drink	424-428
29	Tobacco	429
30	Textiles	431-439
31	Leather and Leather Goods	441-442
32	Footwear	451
33	Clothing	453
34	Household Textiles and Fur	455-456
35	Timber and Wooden Products	461-466
36	Furniture	467
37	Pulp, Paper and Board	471-472
38	Printing and Publishing	475
39	Rubber Products	481-482
40	Plastic Products	483
41	Other Manufacturing	491-495

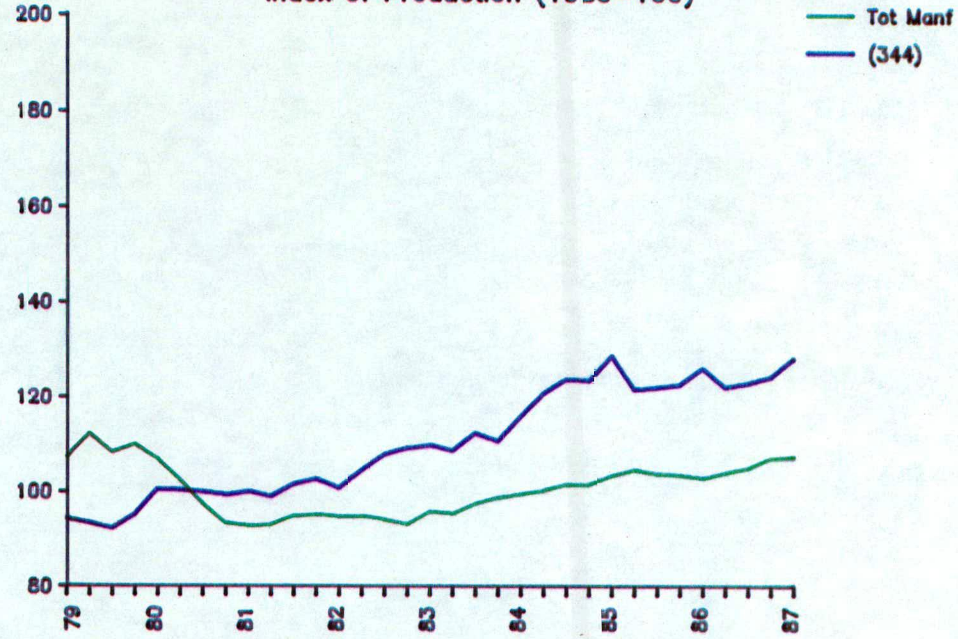
MOVEMENTS IN THE INDEX OF PRODUCTION SINCE 1979

This annex presents charts of movements in the index of production since the beginning of 1979 for each of the 41 sectors identified. A plot of movements in the index of total manufacturing output is included on each chart as a reference point. To aid comparison, the same scale is used for most charts. For sectors where experience differed widely from the average for all manufacturing a different scale is used. The charts are presented in the same order as the listing in Tables 1 and 2 ie in order of output growth.

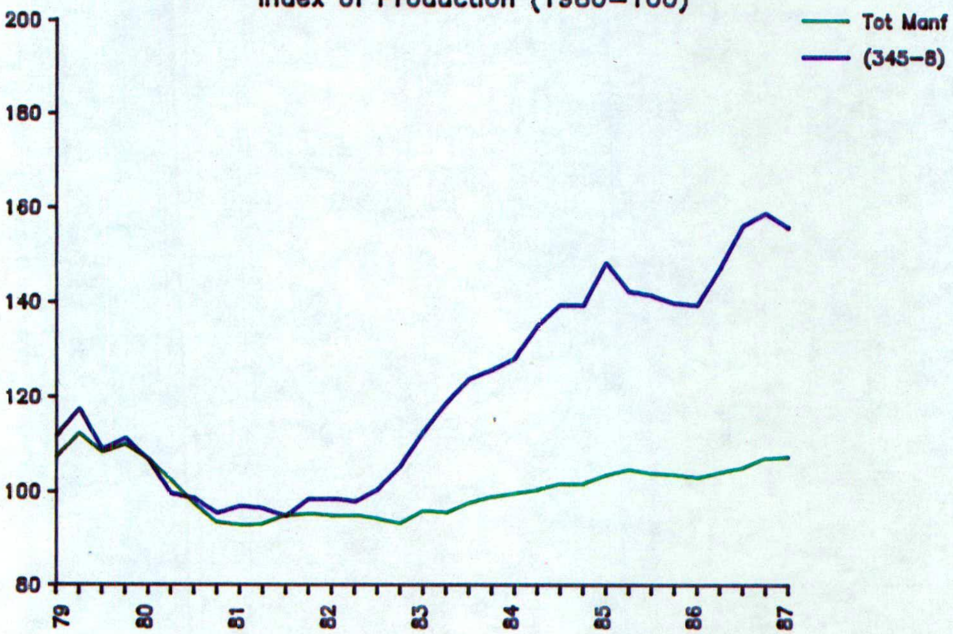
18 Office Mchnry, Computers (33)
Index of Production (1980=100)



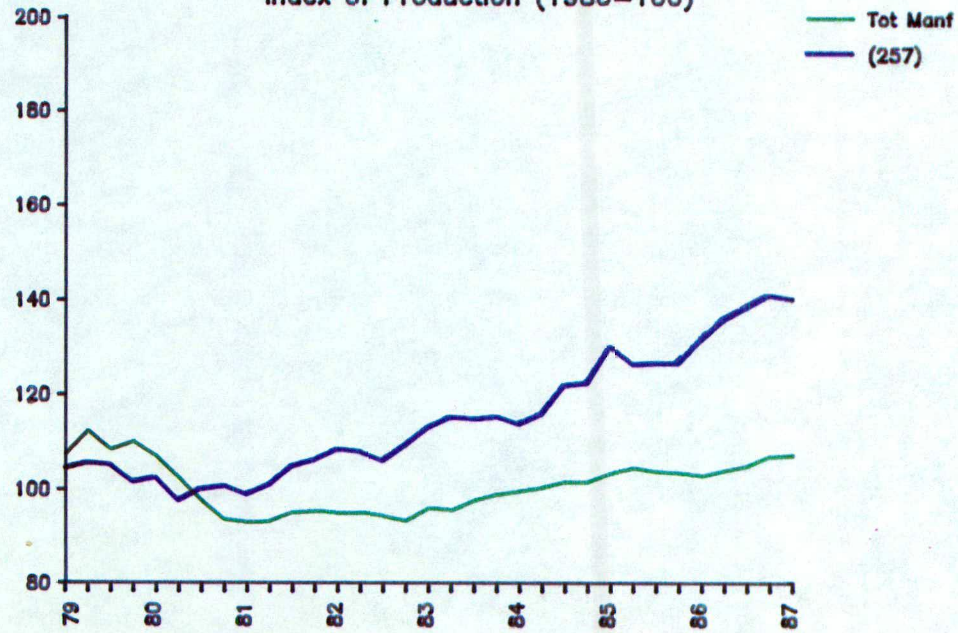
20 Telecomms etc Eqt (344)
Index of Production (1980=100)



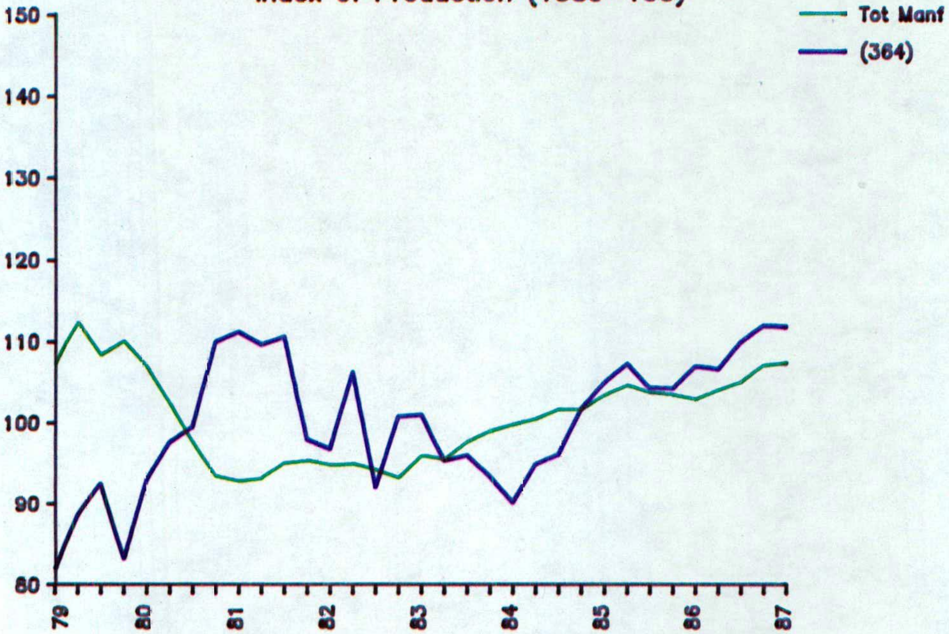
21 Electrical Consumr Gds (345–8)
Index of Production (1980=100)



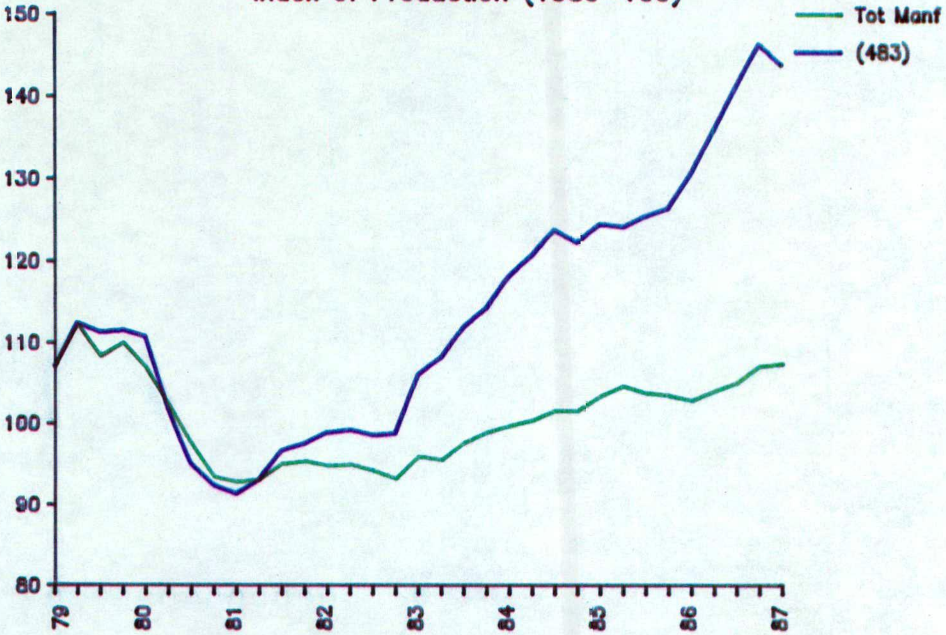
8 Pharmaceuticals (257)
Index of Production (1980=100)



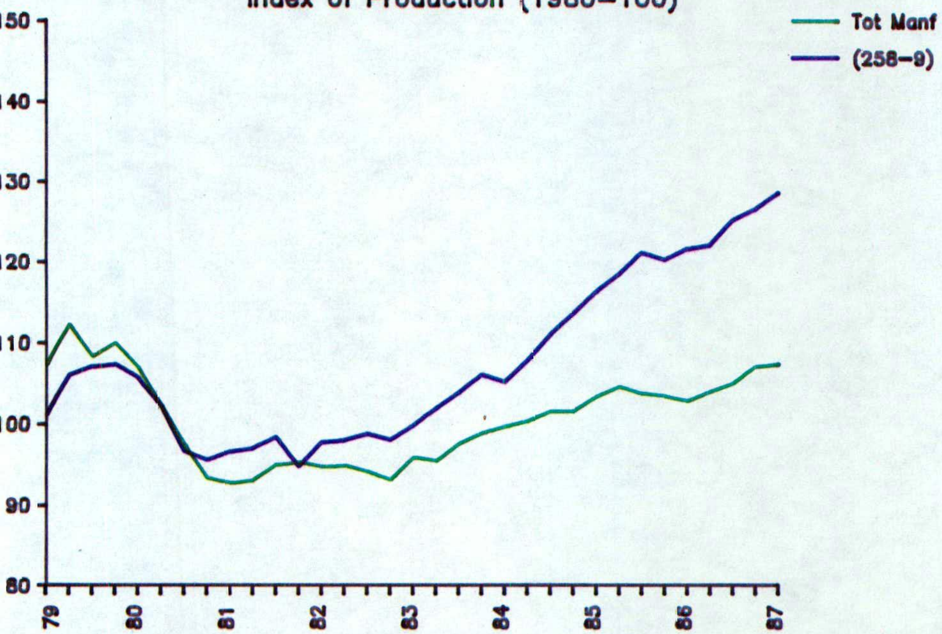
24 Aerospace (364)
Index of Production (1980=100)



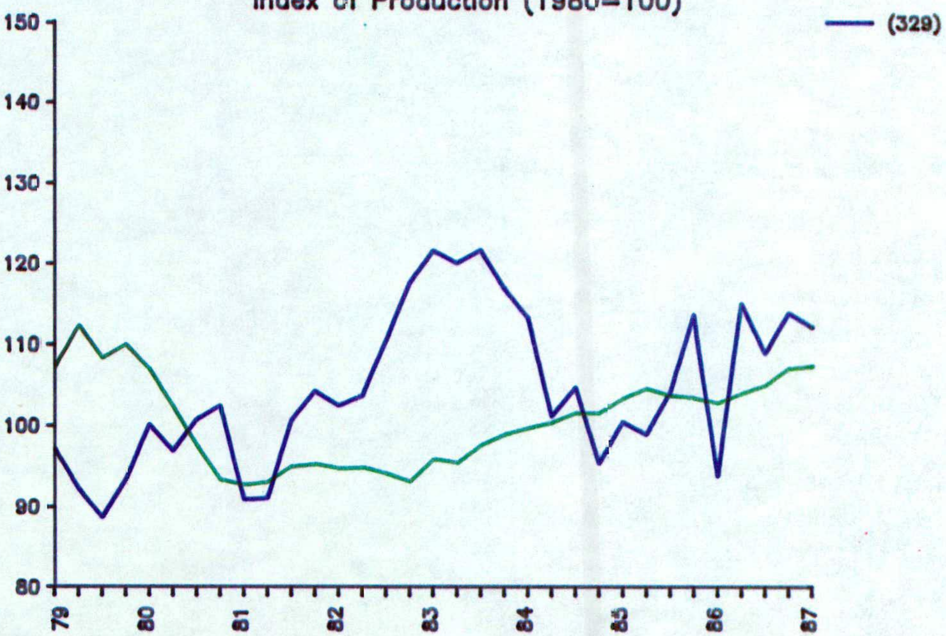
40 Plastic Products (483)
Index of Production (1980=100)

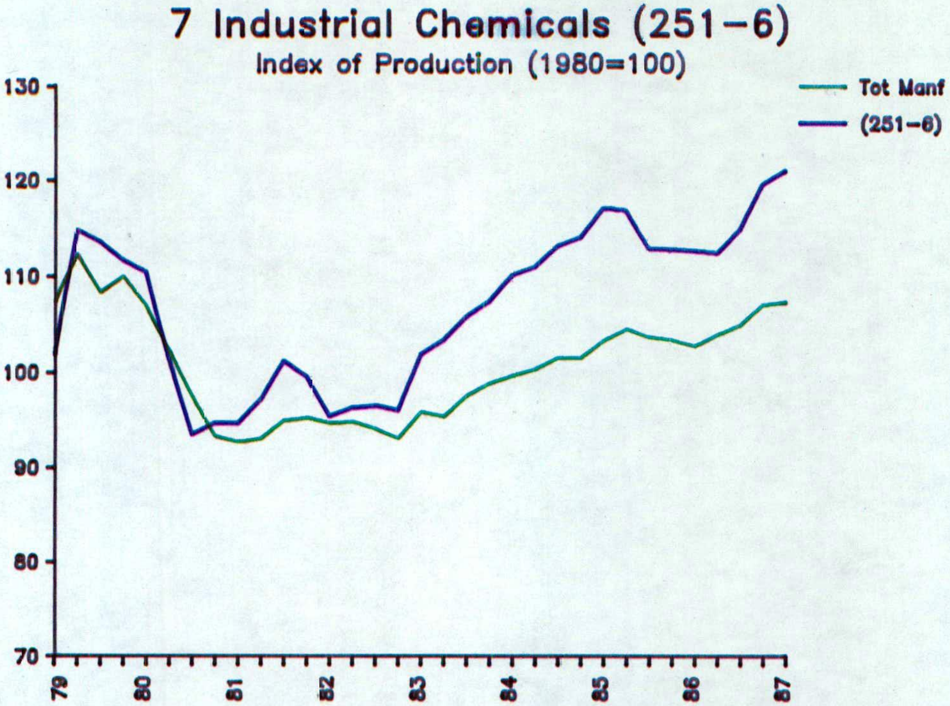


9 Consumer Chemicals (258-9)
Index of Production (1980=100)



17 Ordnance & Small Arms (329)
Index of Production (1980=100)





7 Industrial Chemicals (251-6)
Index of Production (1980=100)
Tot Manf
(251-6)
130
120
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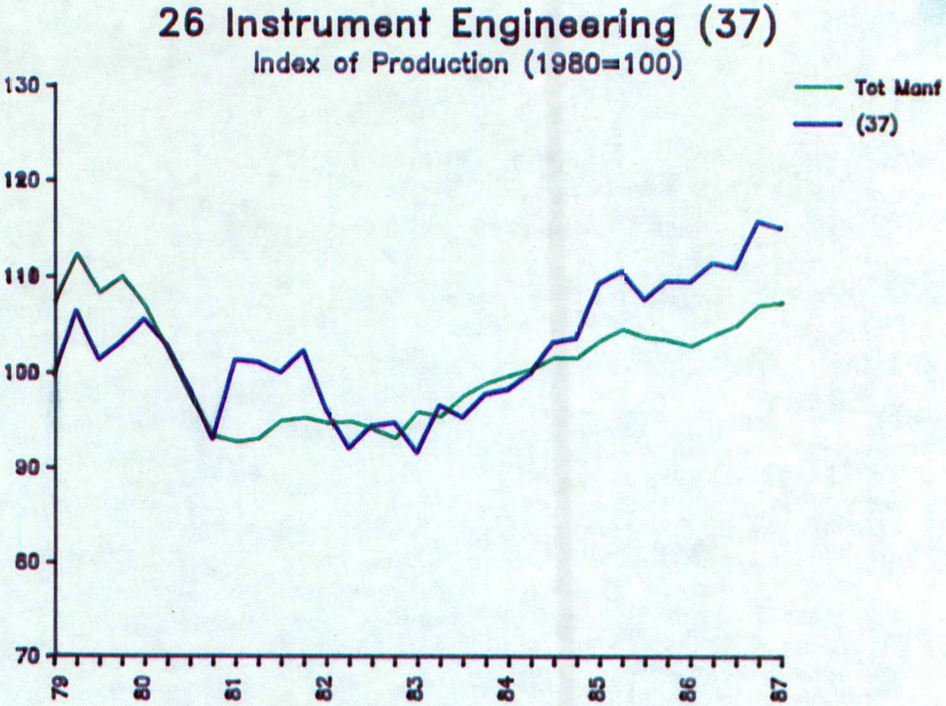

26 Instrument Engineering (37)
Index of Production (1980=100)
Tot Manf
(37)
130
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100
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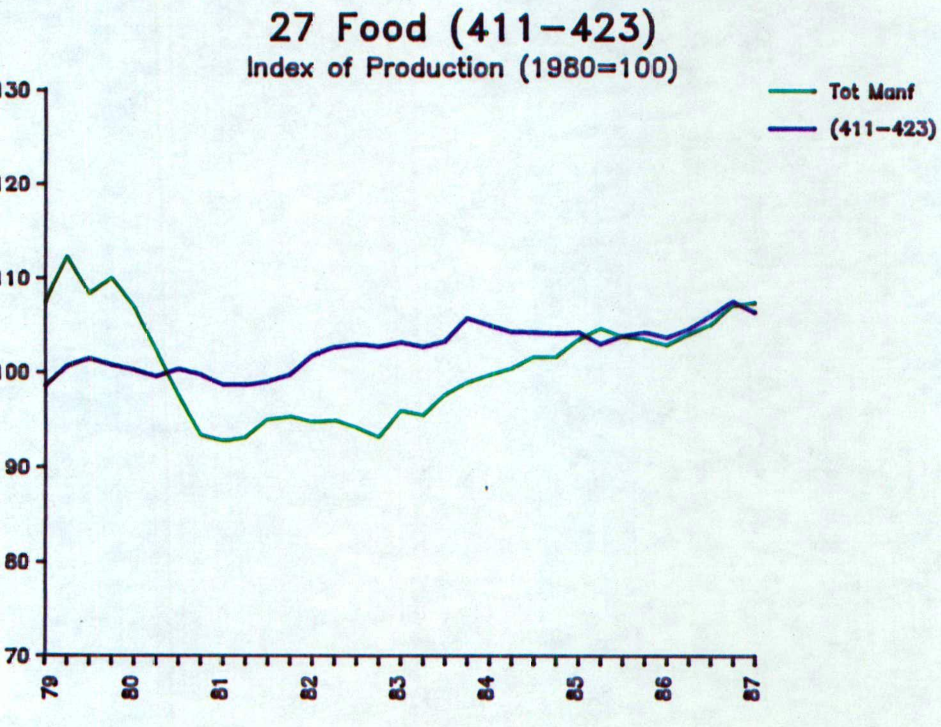

27 Food (411-423)
Index of Production (1980=100)
Tot Manf
(411-423)
130
120
110
100
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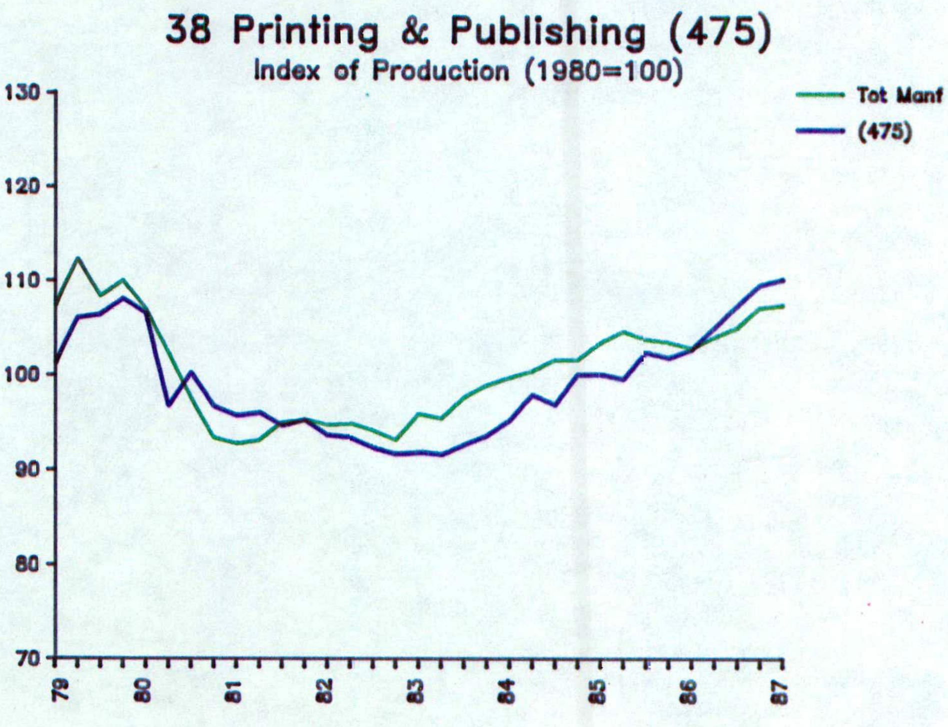

38 Printing & Publishing (475)
Index of Production (1980=100)
Tot Manf
(475)
130
120
110
100
90
80
70
79
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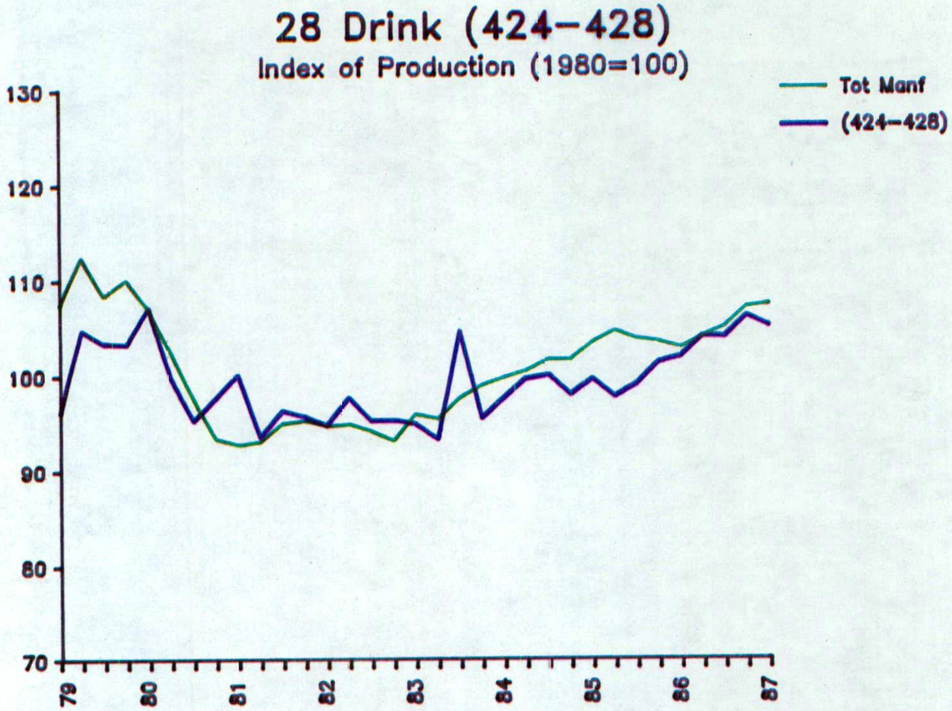
81
82
83
84
85
86
87


28 Drink (424–428)
Index of Production (1980=100)
Tot Manf
(424–428)
130
120
110
100
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80
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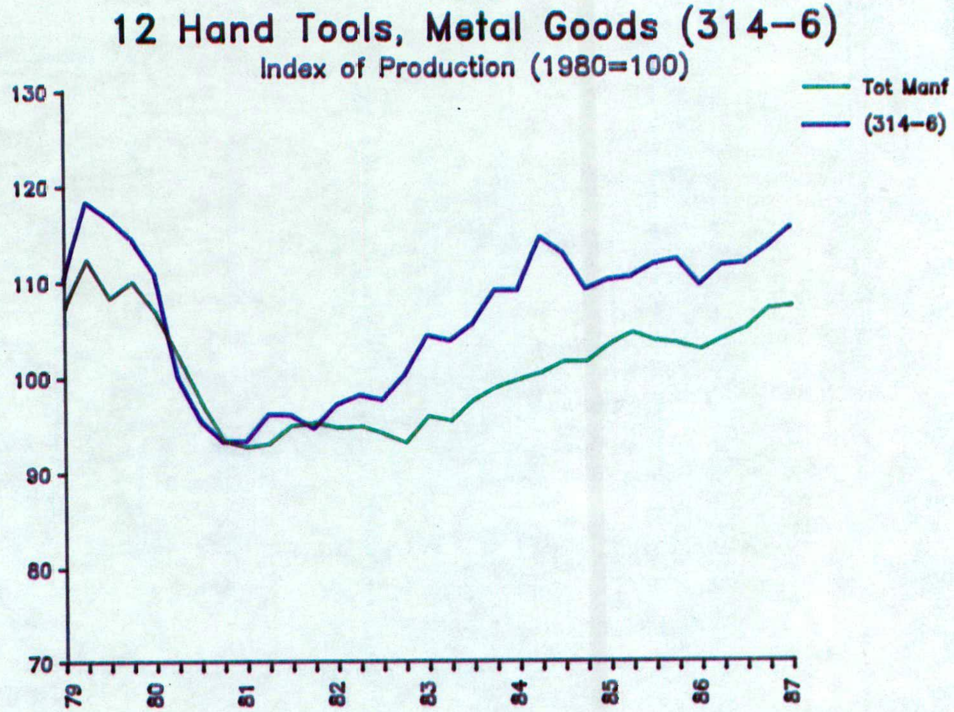
12 Hand Tools, Metal Goods (314–6)
Index of Production (1980=100)
Tot Manf
(314–6)
130
120
110
100
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79
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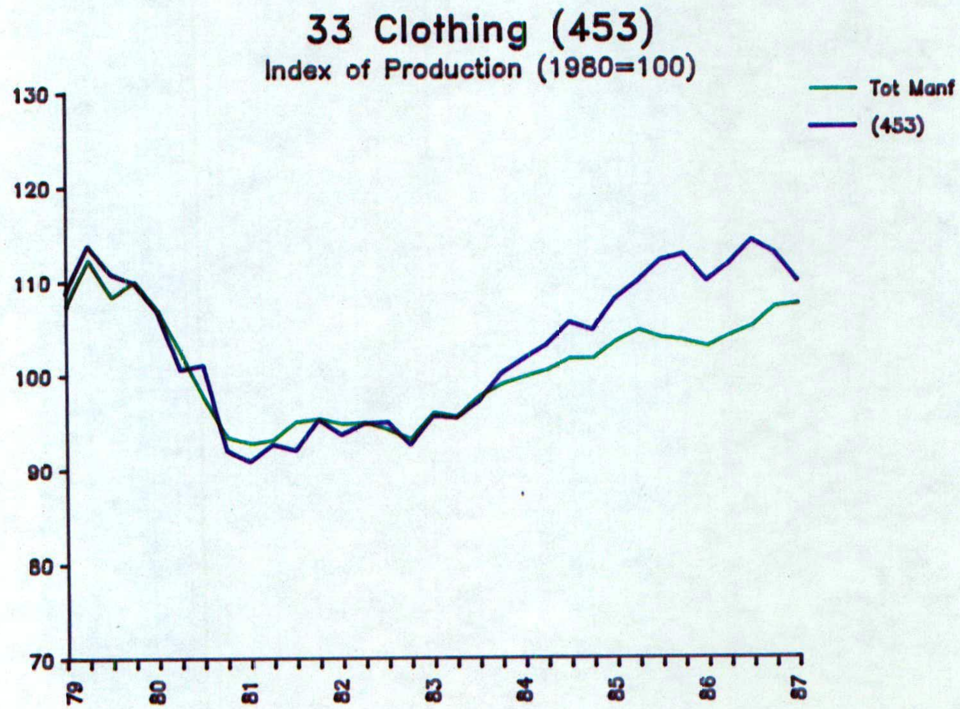
33 Clothing (453)
Index of Production (1980=100)
Tot Manf
(453)
130
120
110
100
90
80
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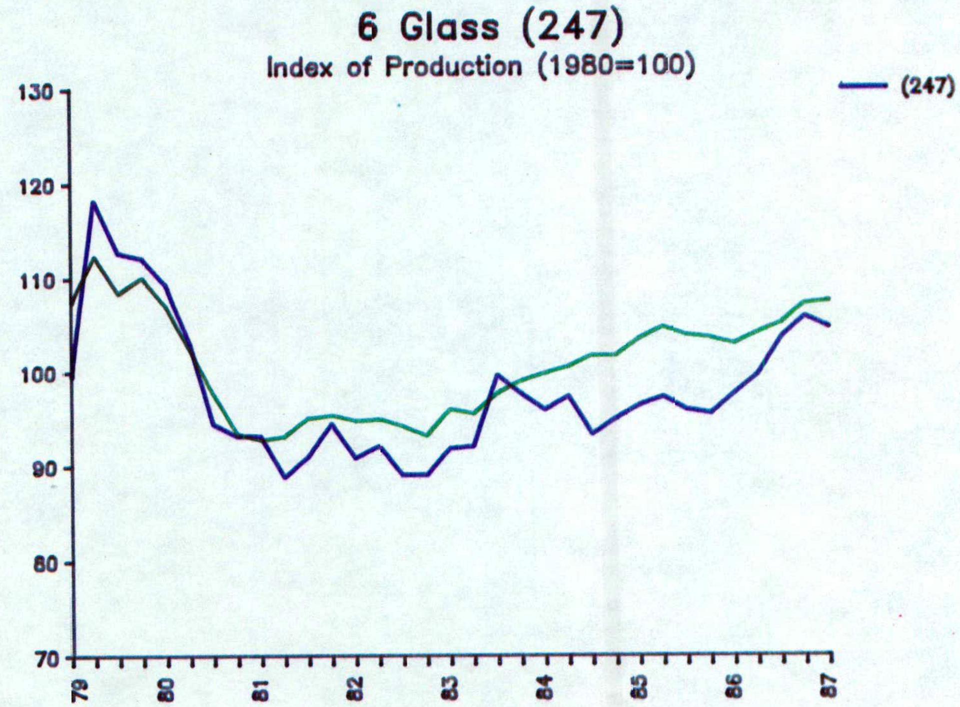
6 Glass (247)
Index of Production (1980=100)
(247)
130
120
110
100
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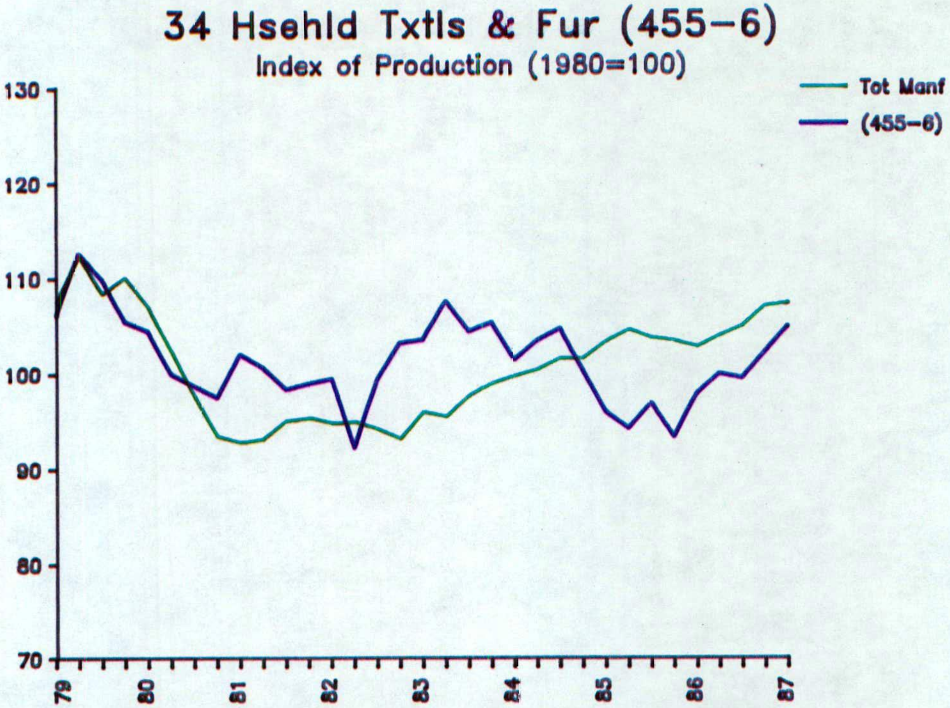
34 Hsehld Txtls & Fur (455-6)
Index of Production (1980=100)
Tot Manf
(455-6)
130
120
110
100
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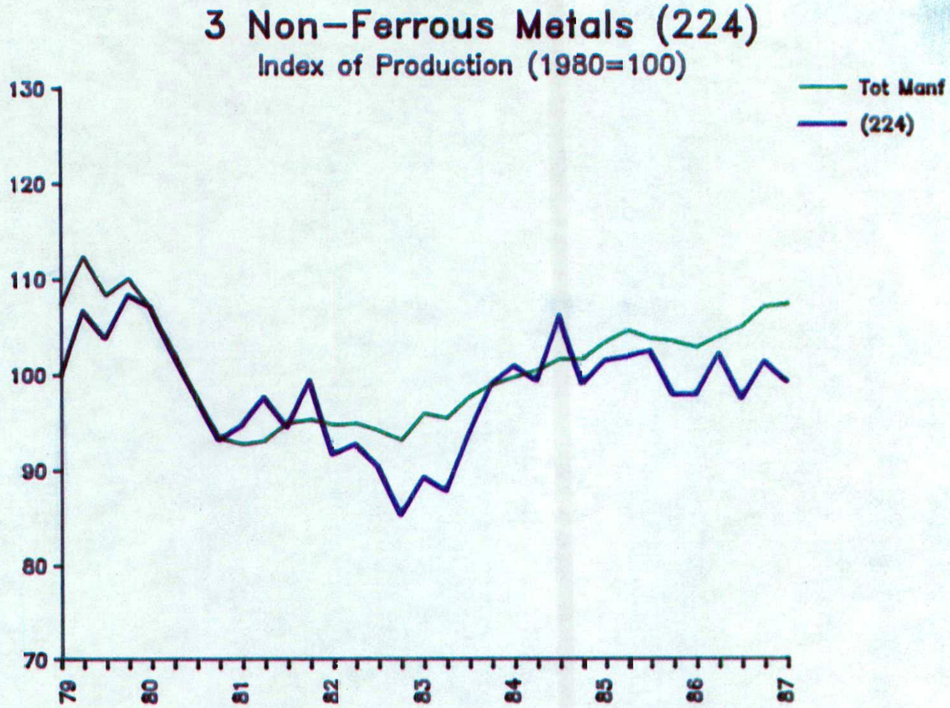
3 Non-Ferrous Metals (224)
Index of Production (1980=100)
Tot Manf
(224)
130
120
110
100
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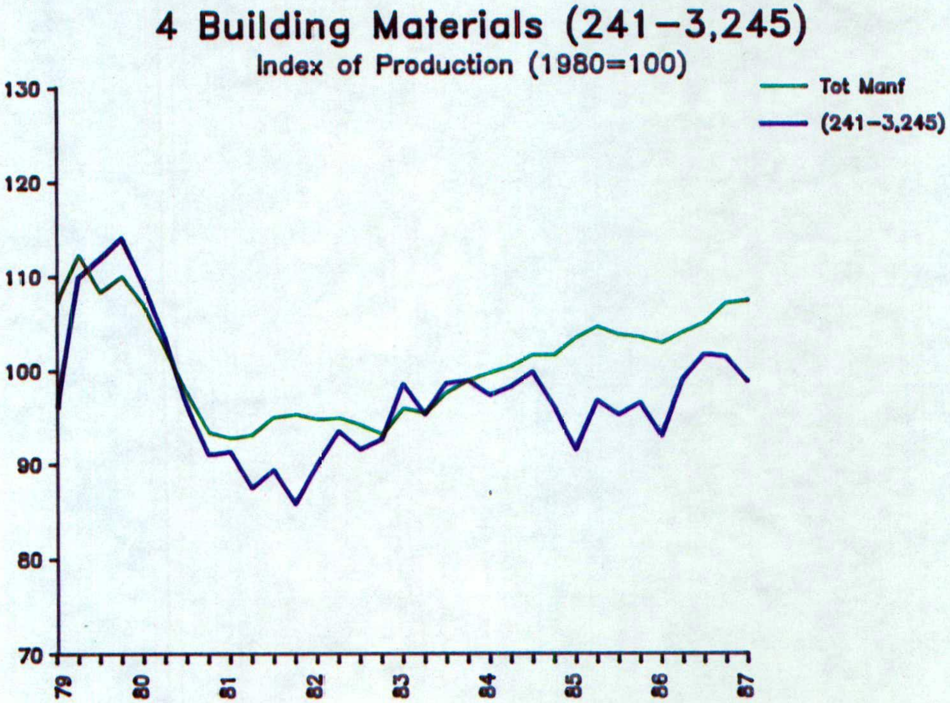
4 Building Materials (241-3,245)
Index of Production (1980=100)
Tot Manf
(241-3,245)
130
120
110
100
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80
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81
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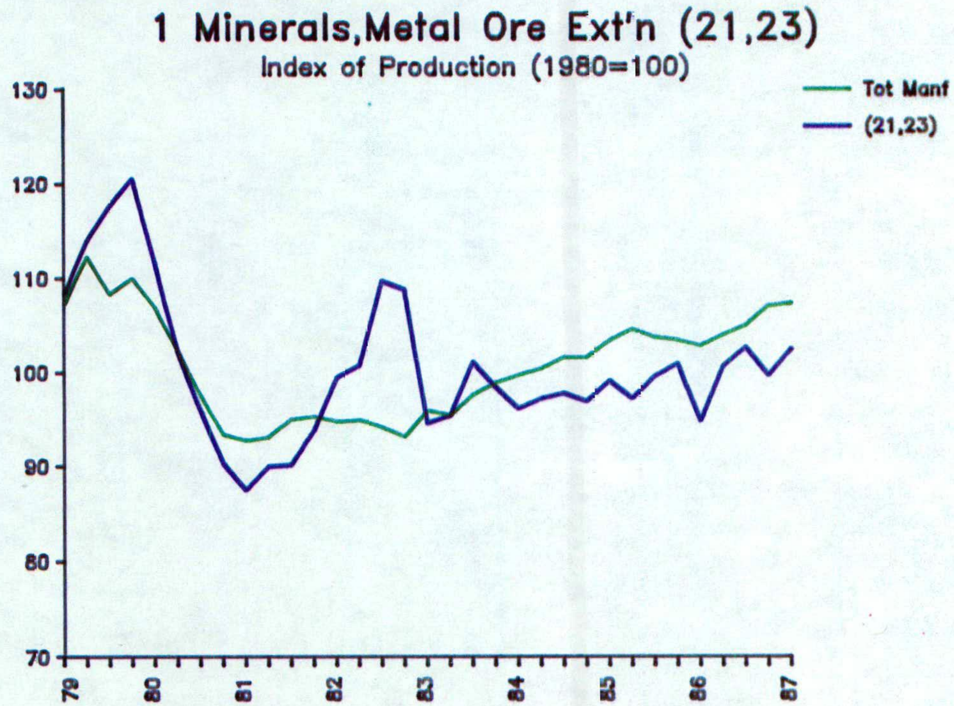
1 Minerals,Metal Ore Ext'n (21,23)
Index of Production (1980=100)
Tot Manf
(21,23)
130
120
110
100
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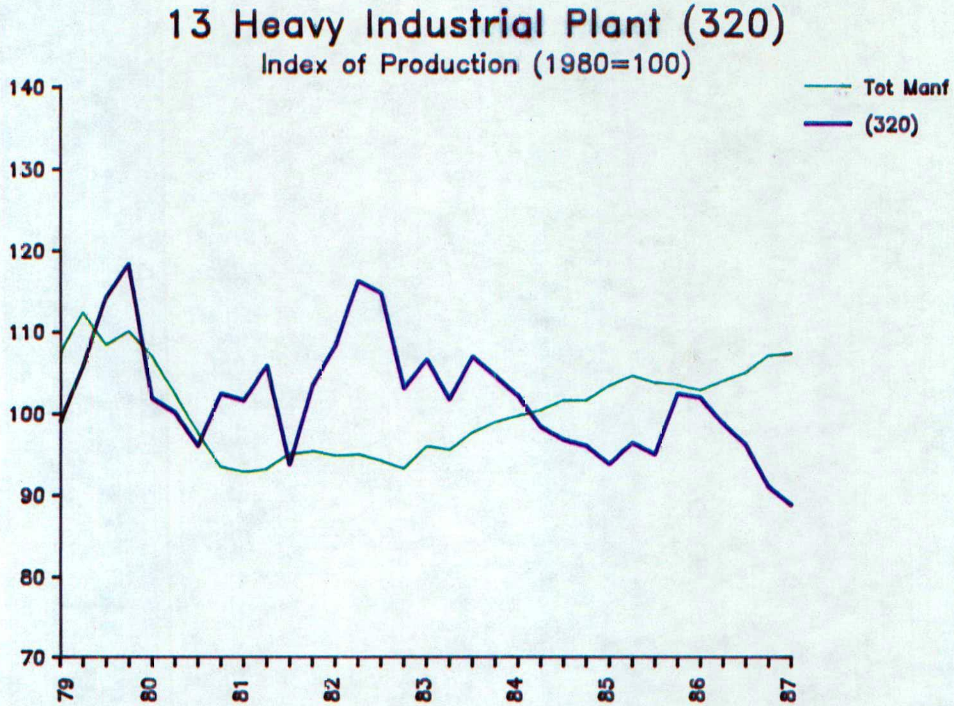
13 Heavy Industrial Plant (320)
Index of Production (1980=100)
Tot Manf
(320)
140
130
120
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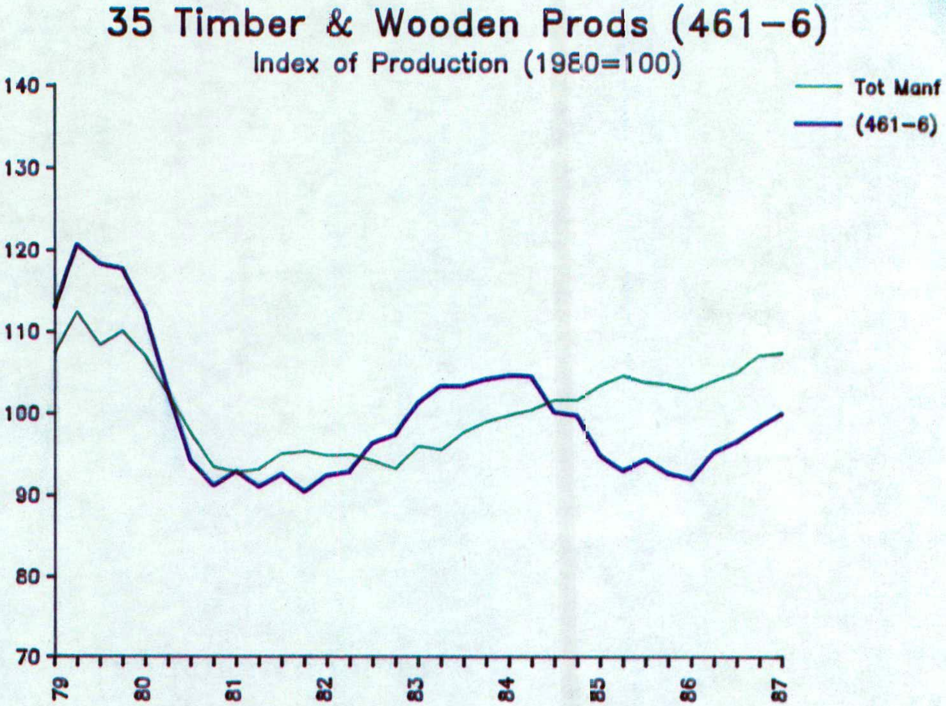
35 Timber & Wooden Prods (461-6)
Index of Production (1980=100)
Tot Manf
(461-6)
140
130
120
110
100
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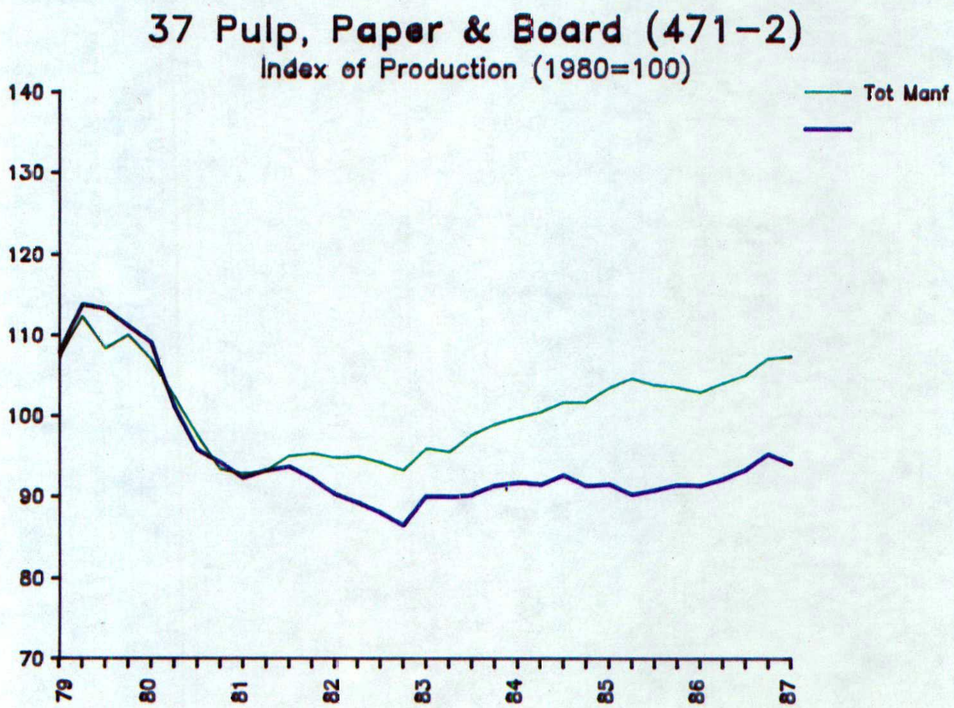
37 Pulp, Paper & Board (471-2)
Index of Production (1980=100)
Tot Manf
140
130
120
110
100
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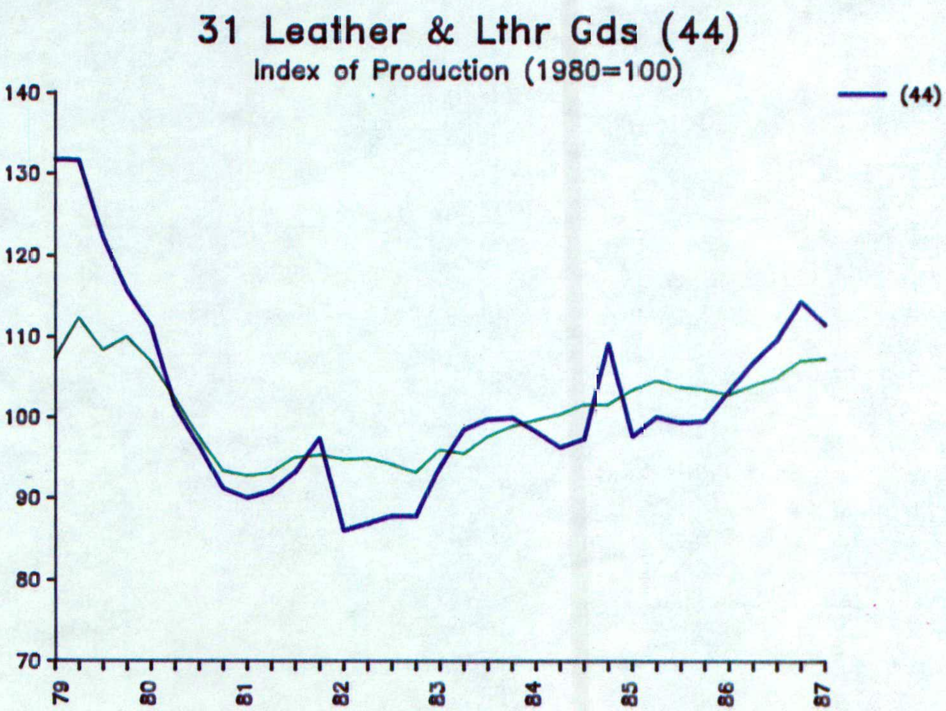
31 Leather & Lthr Gds (44)
Index of Production (1980=100)
(44)
140
130
120
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100
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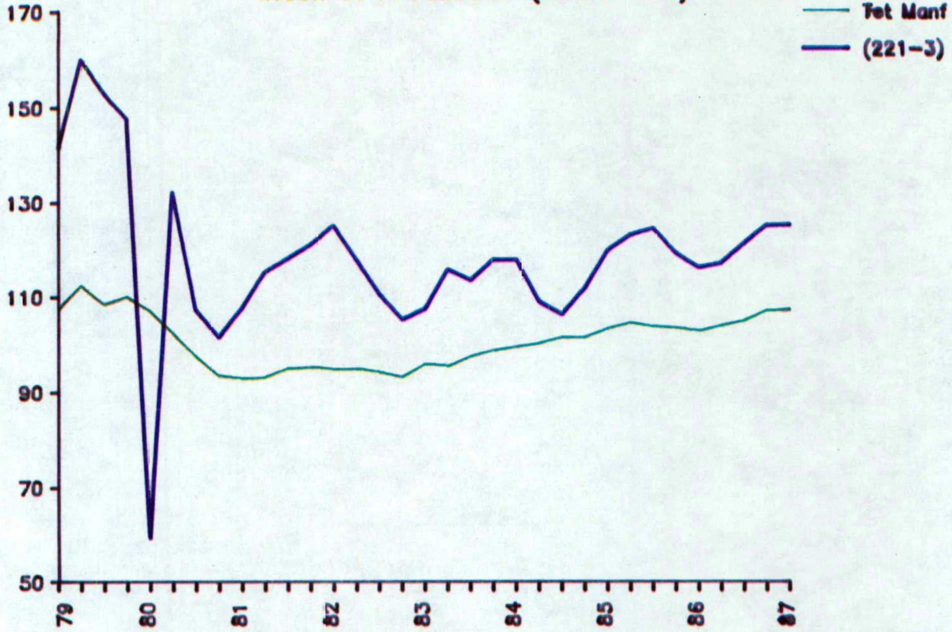
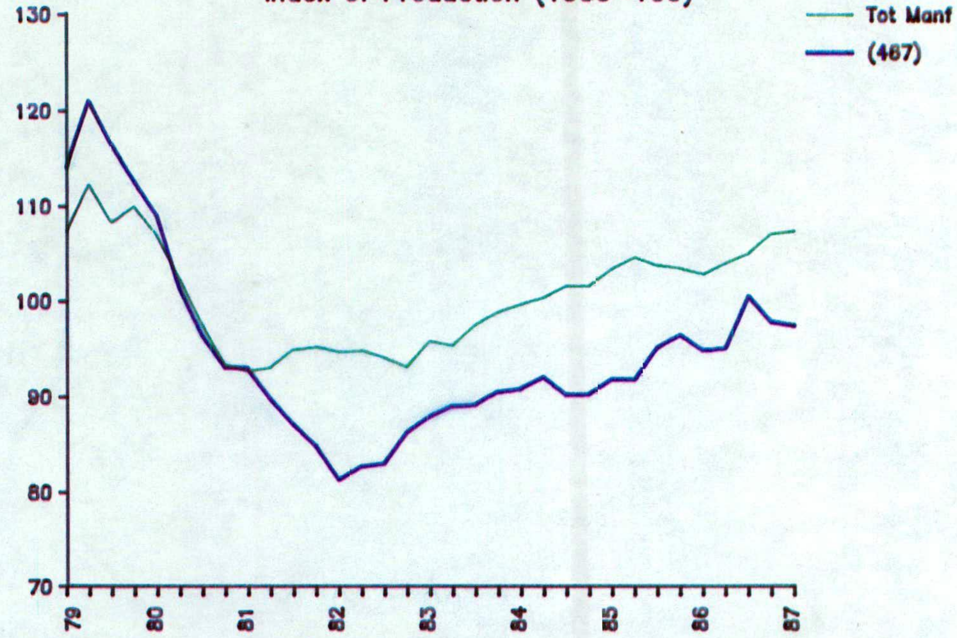
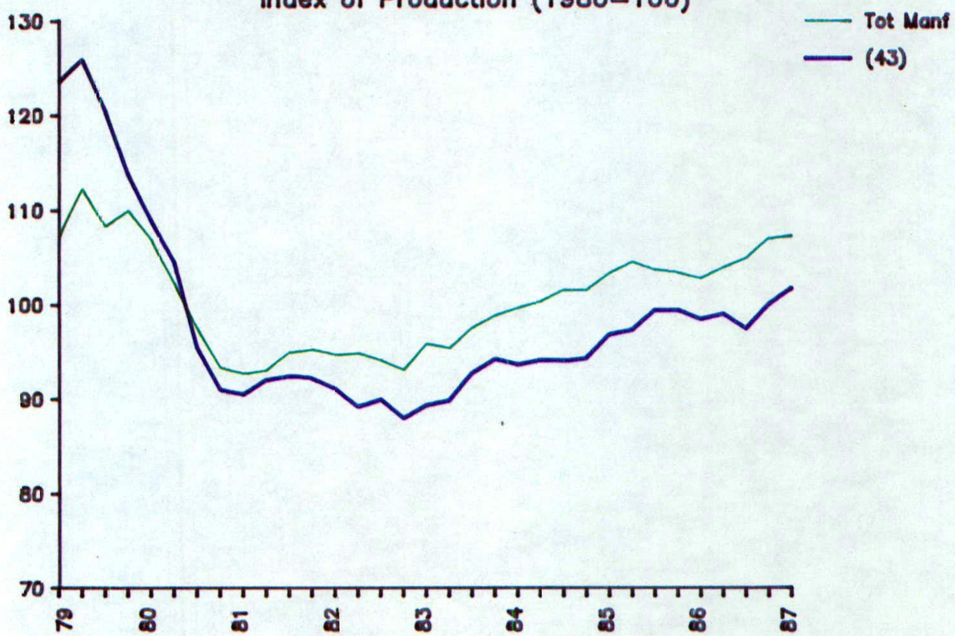
2 Ferrous Metals (221-3)
Index of Production (1980=100)



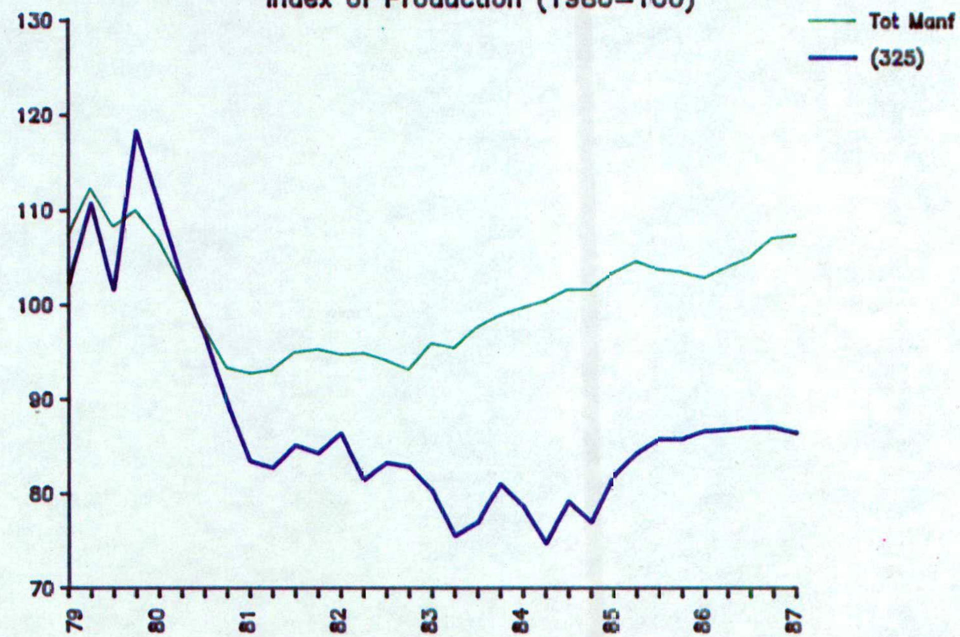
36 Furniture (467)
Index of Production (1980=100)



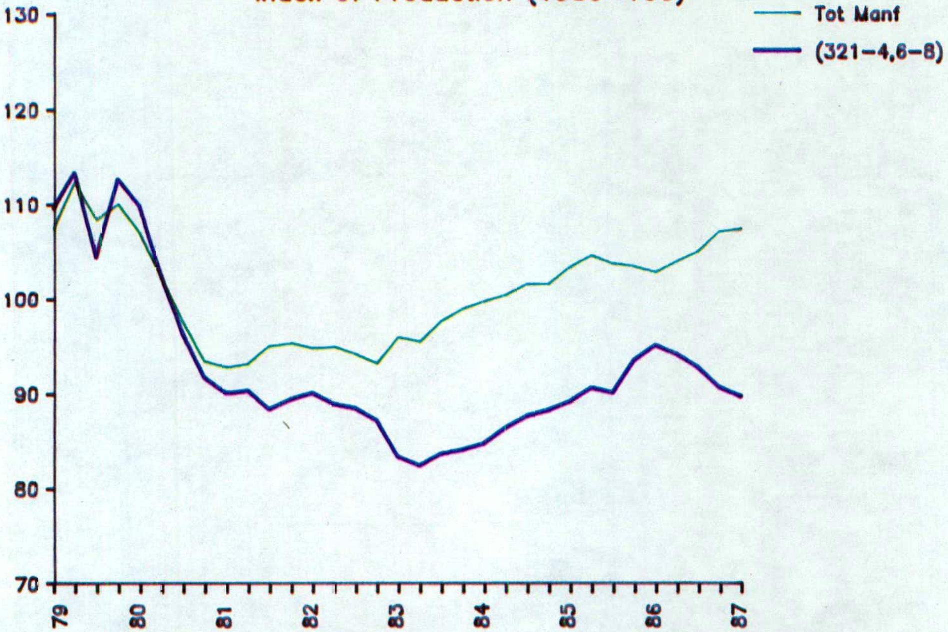
30 Textiles (43)
Index of Production (1980=100)



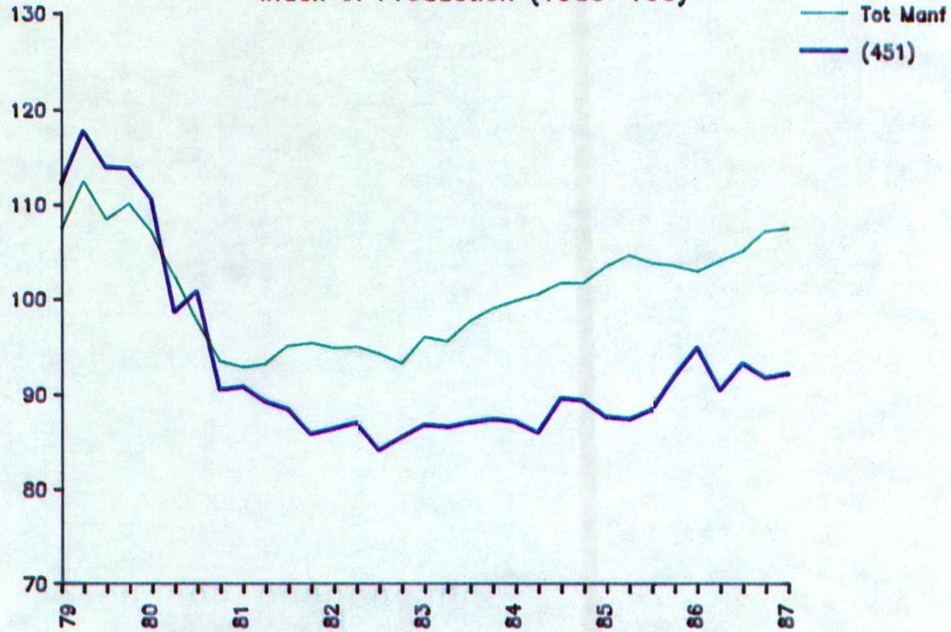
15 Mining & Constrctn Eqt (325)
Index of Production (1980=100)



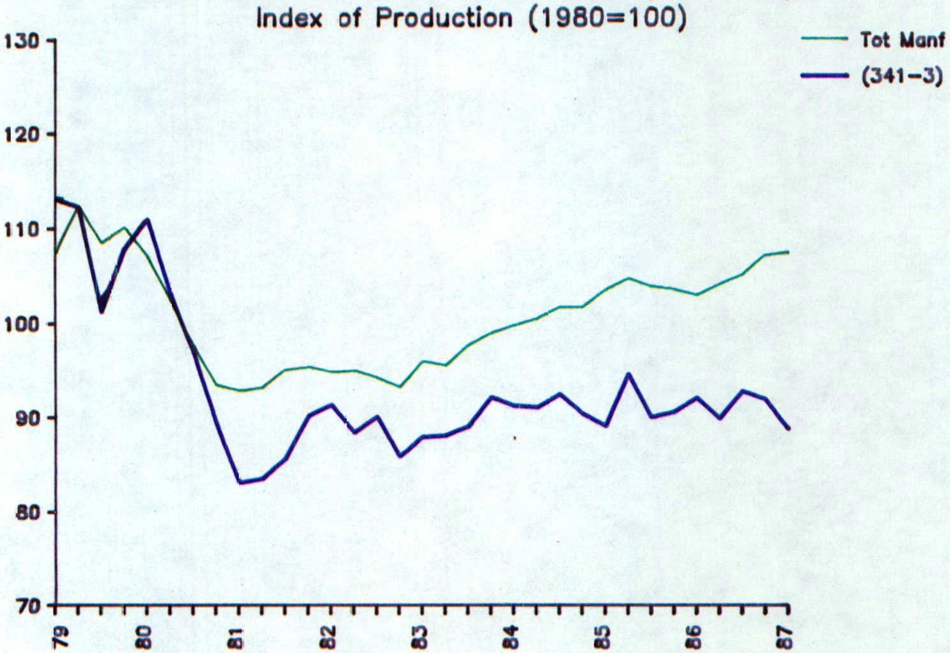
16 Other Machinery (321,3,4,6,7,8)
Index of Production (1980=100)



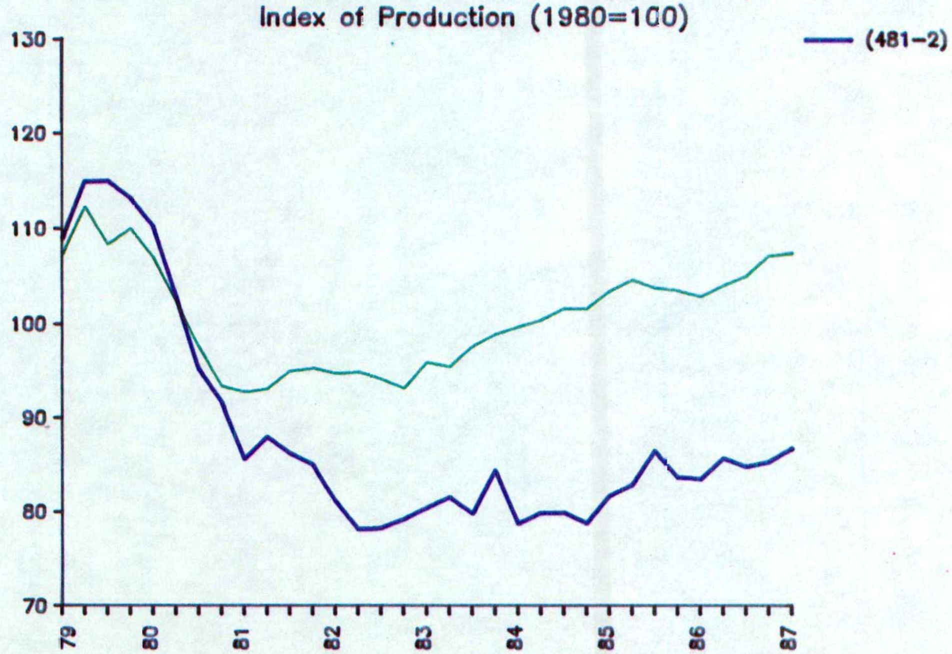
32 Footwear (451)
Index of Production (1980=100)



19 Electrical Indstrl Gds (341-3)
Index of Production (1980=100)

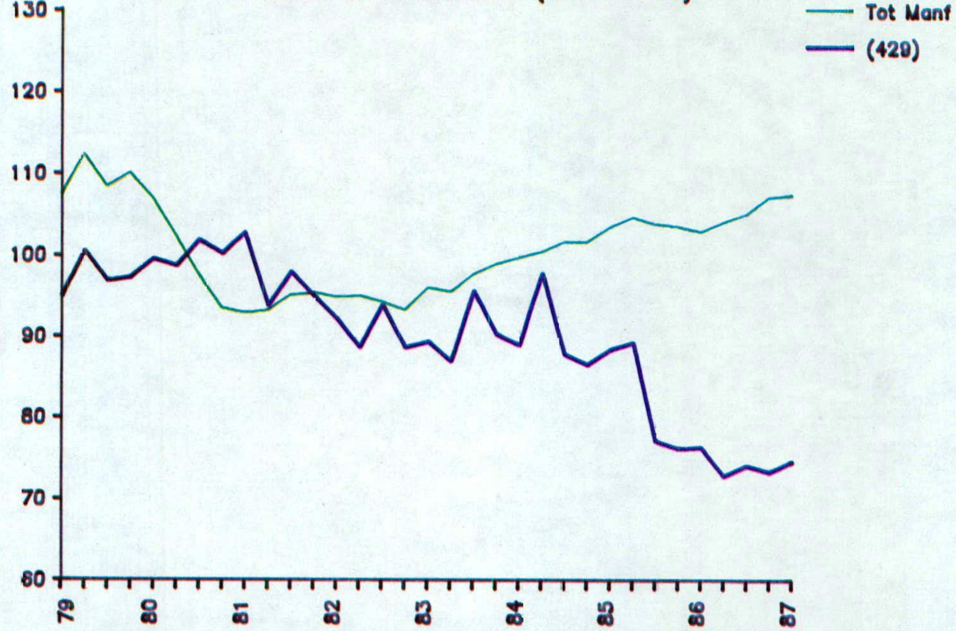


39 Rubber Products (481-2)
Index of Production (1980=100)



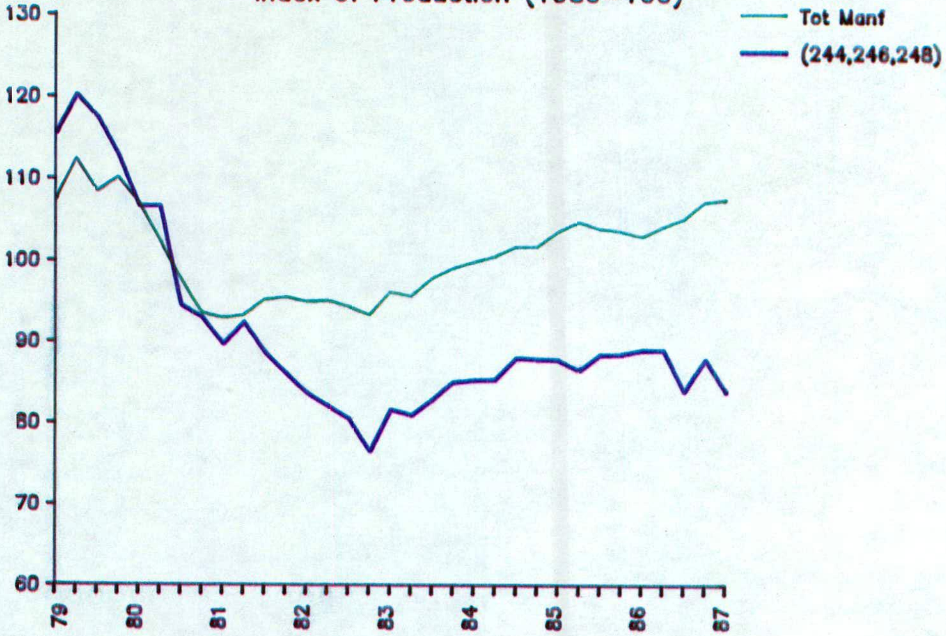
29 Tobacco (429)

Index of Production (1980=100)



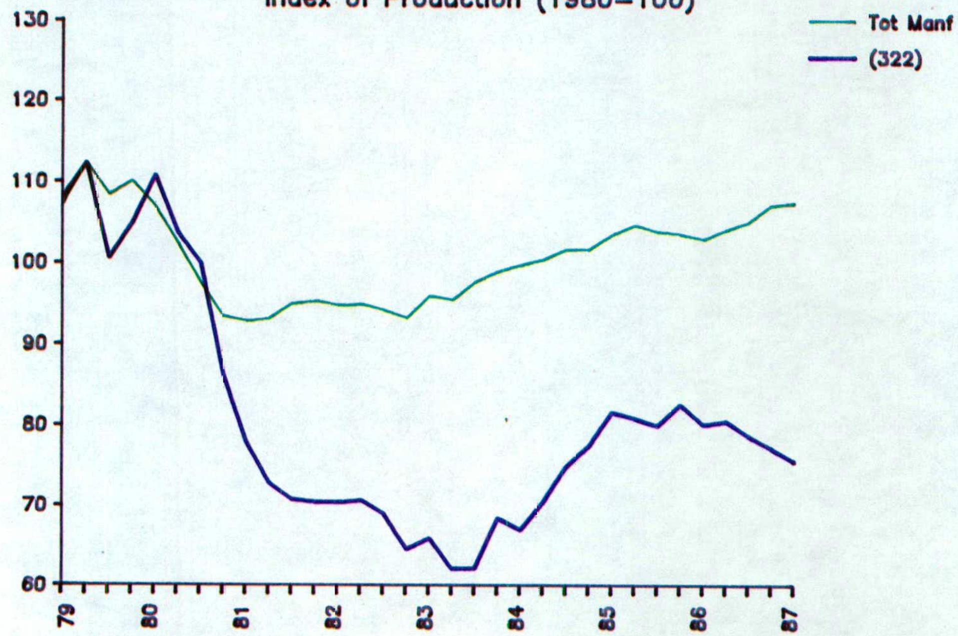
5 Ceramics,Abrasives etc (244,246,248)

Index of Production (1980=100)



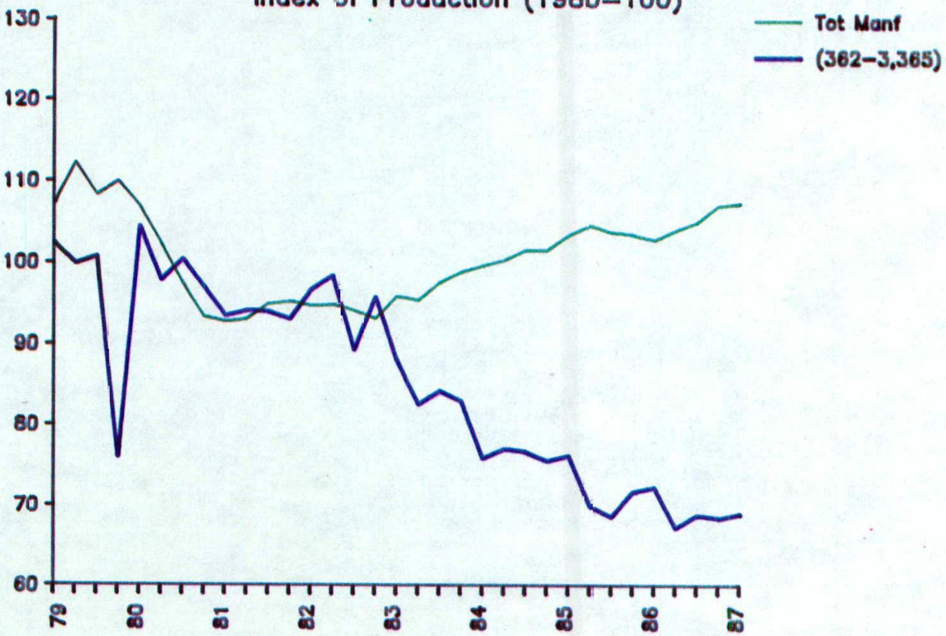
14 Metal–Working Machine Tools (322)

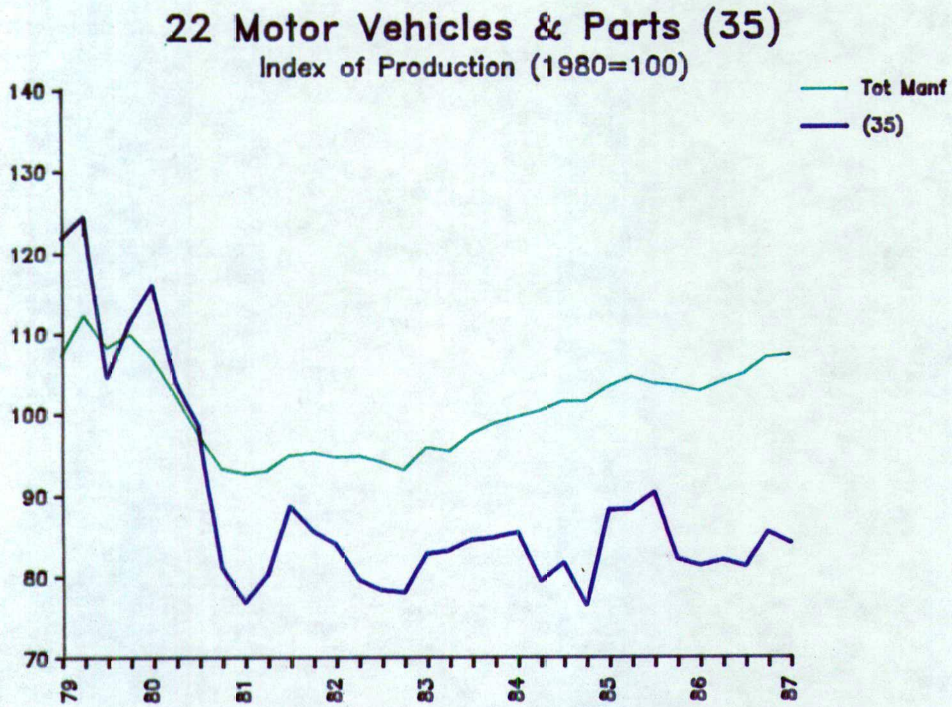
Index of Production (1980=100)



25 Other Vehicles (362–3,365)

Index of Production (1980=100)




22 Motor Vehicles & Parts (35)
Index of Production (1980=100)
Tot Manf
(35)
140
130
120
110
100
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80
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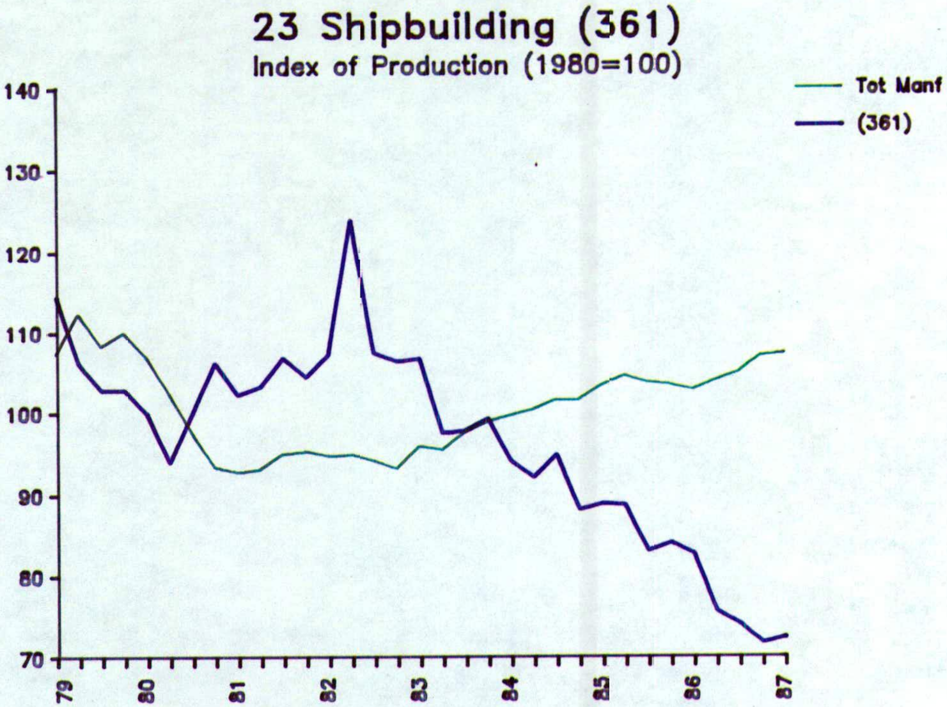
23 Shipbuilding (361)
Index of Production (1980=100)
Tot Manf
(361)
140
130
120
110
100
90
80
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84
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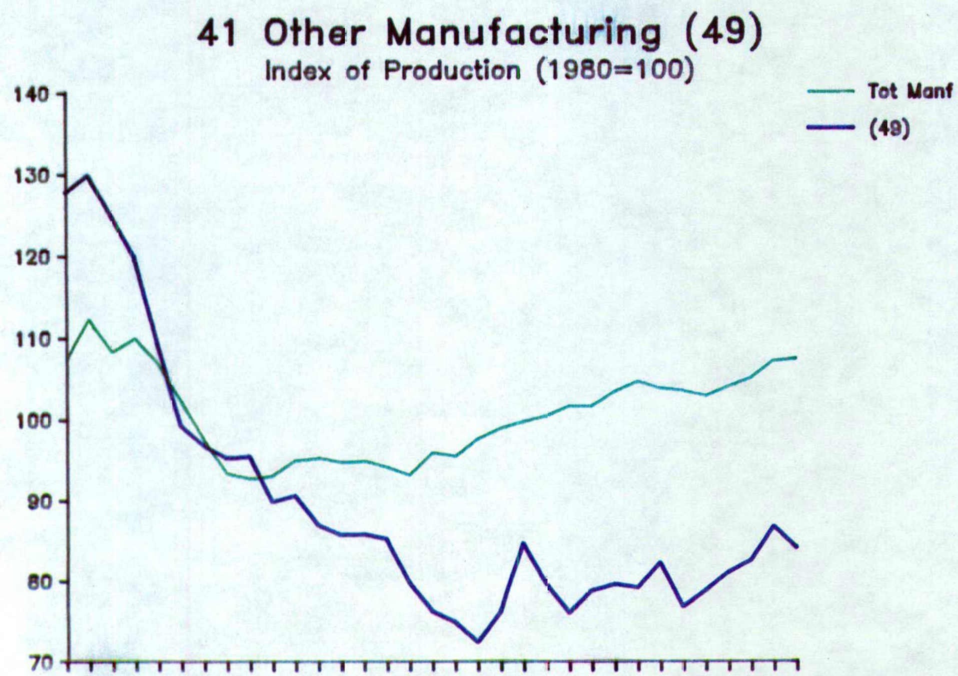
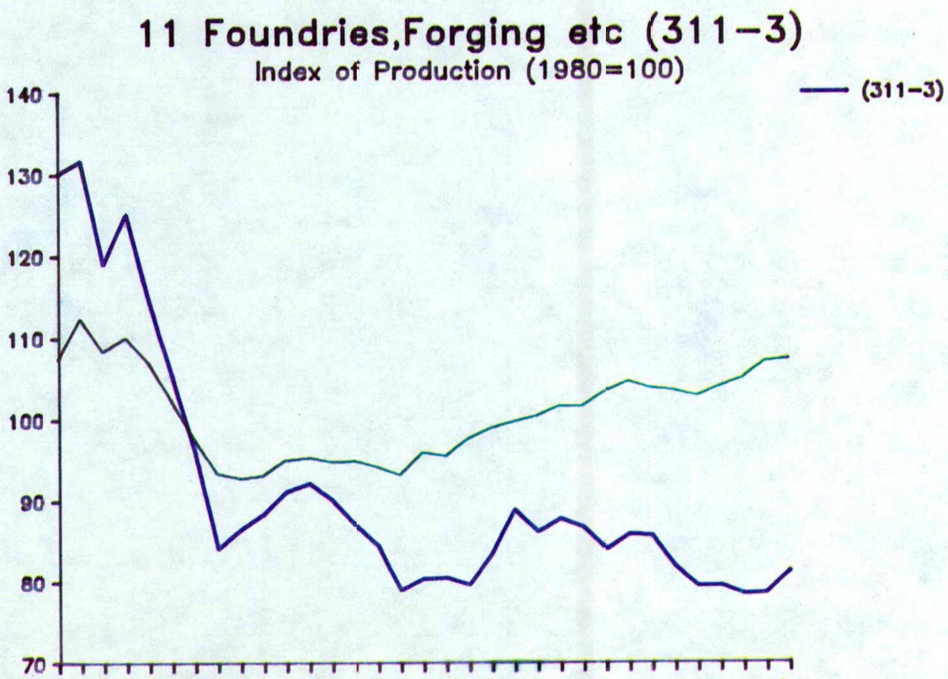
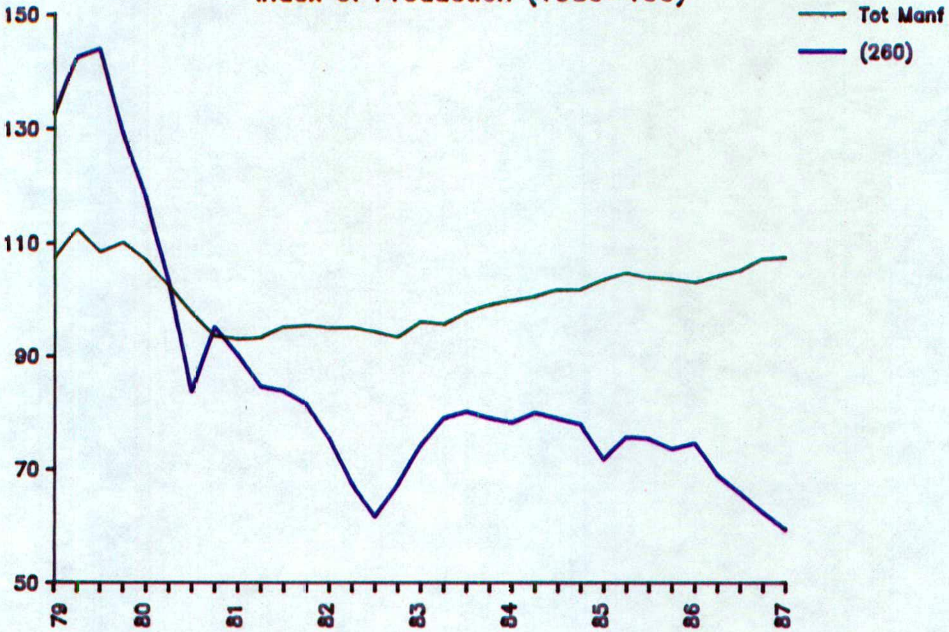

41 Other Manufacturing (49)
Index of Production (1980=100)
Tot Manf
(49)
140
130
120
110
100
90
80
70


11 Foundries,Forging etc (311-3)
Index of Production (1980=100)
(311-3)
140
130
120
110
100
90
80
70

10 Man-Made Fibres (260)

Index of Production (1980=100)



PERCENTAGE CHANGE IN VOLUME OF EXPORTS AND IMPORTS BETWEEN THE YEARS ENDING 1979Q2 AND 1986Q4

	Exports	Imports
Computers and other office machinery	202	295
Electronic capital goods (inc. Telecommunications)	66	116
Electrical consumer goods	43	162
Pharmaceuticals	40	92
Aerospace	84	49
Plastic products	43	104
Consumer chemicals	71	244
Ordnance and small arms	36	59
Industrial chemicals	33	49
Instrument engineering	20	105
Food	34	14
Printing and publishing	11	101
Drink	- 8	59
Hand tools and finished metal goods	- 6	68
Clothing	12	45
Glass	12	59
Household textiles and fur	1	36
Non-Ferrous metals	35	33
Building materials	65	133
Extraction of minerals and metal ores	- 20	- 22
Heavy industrial plant	- 42	- 1
Timber and wooden products	- 19	8
Pulp, paper and board	40	43
Leather and leather goods	10	33
Ferrous metals	30	36
Furniture	- 15	116
Textiles	- 4	37
Mining, construction and associated equipment	- 10	13
Other machinery	- 9	39
Footwear	- 1	52
Electrical industrial goods	- 1	91
Rubber products	8	73
Tobacco	- 1	185
Ceramics, abrasives and asbestos	- 15	64
Metal-working machine tools	- 4	30
Other vehicles	- 38	- 26
Motor vehicles and parts	- 26	42
Shipbuilding	- 59	61
Other manufacturing	- 20	- 16
Basic metal forming	- 25	34
Man-made fibres	- 27	10
Total Manufacturing	16	50

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To: MINISTER FOR TRADE

Copy No. (3) 28

From: W E BOYD
S2A
V/286 Ext. 4887

5 August 1987

OVERSEAS TRADE FIGURES FOR JUNE 1987

THE CURRENT ACCOUNT

In June, exports were valued at £6.4 billion and imports at £7.1 billion so that visible trade, seasonally adjusted on a balance of payments basis, showed a deficit of £0.8 billion compared with a deficit of £1.1 billion in May.

The Central Statistical Office project a surplus on invisibles of £0.6 billion for June so that the current account is provisionally estimated to have been in deficit by £0.2 billion in June compared with a deficit of £0.5 billion in May.

TABLE 1: CURRENT BALANCE, VISIBLE TRADE AND INVISIBLES
(Table 2 of Press Notice)

Seasonally adjusted
Balance of Payments
Basis
£ million

	Current Account Balance	Visible Trade Balances			Invisibles Balance
		Total	Oil	Non-oil	
1985	+3450	-2178	+8104	+10282	+5628
1986	- 120	-8253	+4153	-12407	+8133
1987 Q1	+ 667	-1135	+1164	- 2300	+1802
Q2	- 630A	-2430	+1022	- 3452	+1800A
1987 April	+ 64A	- 536A	+ 419	- 955	+ 600A
May	- 527A	-1127A	+ 361	- 1488	+ 600A
June	- 168A	- 768A	+ 242	- 1009	+ 600A

A = Projection

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In the second quarter of 1987 there was a deficit on visible trade of £2.4 billion - a surplus on trade in oil of £1.0 billion offset by a deficit on non-oil trade of £3.5 billion. Between the first and second quarters of the year, the visible trade balance deteriorated by £1.3 billion - the surplus on oil fell by £0.1 billion while the deficit on non-oil trade rose by £1.2 billion.

EXPORTS

The value of exports in June was £26 million (½ per cent) higher than in May. Exports of both oil and of the erratic items were little changed in June so that excluding these, exports also rose by about ½ per cent between May and June.

In the second quarter of this year, total export volume was 3 per cent lower than in the previous three months and 3½ per cent higher than in the second quarter of last year. Excluding oil and the erratic items export volume decreased by 1½ per cent between the first and second quarters of this year but stands 6 per cent up on the second quarter of last year. The underlying level of non-oil export volume appears now to have settled at a level a little below that reached at the end of last year.

TABLE 2: EXPORTS BY VALUE AND VOLUME (Tables 1, 4 and 7 of Press Notice)

Bop Basis, Seasonally Adjusted

	VALUE (£m)		VOLUME (1980 = 100)	
	Total	Total Less Oil and erratics	Total	Total less Oil and erratics
1985	78111	57685	118.7	114.9
1986	72843	59238	123.1	117.7
1987 Q1	19637	15899	130.0	124.4
Q2	19323	15864	126.0	122.3
1987 April	6604	5304	131.4	123.5
May	6347	5264	123.5	121.4
June	6373	5296	123.1	122.0

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By value, exports fell by 1½ per cent between the first and second quarters. Exports to the developed countries fell by 1½ per cent and exports to the developing countries increased by 1½ per cent. Within the total for the developed countries, exports to Western Europe grew by 5½ per cent while deliveries to North America were down by 21 per cent.

IMPORTS

The value of imports in June was £333 million (4½ per cent) lower than in May. Imports of oil rose by £105 million and imports of the erratic items rose by £18 million. Excluding oil and the erratic items, imports fell by 6½ per cent between May and June to a level about 1 per cent higher than in April.

Total import volume increased by 5½ per cent between the first and second quarters to be 9 per cent higher than a year earlier. Excluding oil and the erratic items the growth in import volume between the first and second quarters remains 5½ per cent with the second quarter of this year 9½ per cent up on the second quarter of last year. Recent figures of imports have fluctuated so much that the trend is undefined. A tentative broad assessment is that the underlying level during 1987 was flat, slightly below the peak in the last quarter of 1986.

TABLE 3: IMPORTS BY VALUE AND VOLUME (Tables 1, 4 and 7 of Press Notice)

Bop Basis, Seasonally Adjusted

	VALUE (£m)		VOLUME (1980 = 100)	
	Total	Total less oil and erratics	Total	Total less oil and erratics
1985	80289	68719	126.0	142.8
1986	81096	73460	133.9	151.1
1987 Q1	20772	18772	133.2	150.4
Q2	21753	19635	140.2	159.0
1987 April	7140	6341	138.4	153.3
May	7473	6875	144.0	167.3
June	7140	6419	138.7	156.4

By value, imports rose by 4½ per cent between the first and second quarters of this year. Arrivals from the developed countries grew by 5 per cent between the two quarters with imports from Western Europe up 5½ per cent, imports from North America up 7½ per cent and imports from the other developed countries down by 2 per cent. Imports from the developing countries increased by 5½ per cent between the two quarters.

TRADE IN MANUFACTURES

Figures showing trade in manufactures on a balance of payments basis will be released with the June current account figures. In the second quarter, there was a deficit on trade manufactures of £1.9 billion compared with a deficit of £0.7 billion in the first quarter. The deficit on trade in manufactures for the first half of the year stands at £2.6 billion compared with a deficit of £1.9 billion in the first half of 1986.

TABLE 4: TRADE IN MANUFACTURES (SITC 5-8) (Table 16 of Press Notice, quarterly data only)

£ million
Seasonally Adjusted
Balance of Payments Basis

	Exports	Imports	Balance
1985	52271	55273	-3002
1986	54486	59883	-5397
1987 Q1	14664	15400	- 736
Q2	14615	16489	-1873
1987 April	4902	5343	- 441
May	4825	5737	- 912
June	4888	5409	- 521

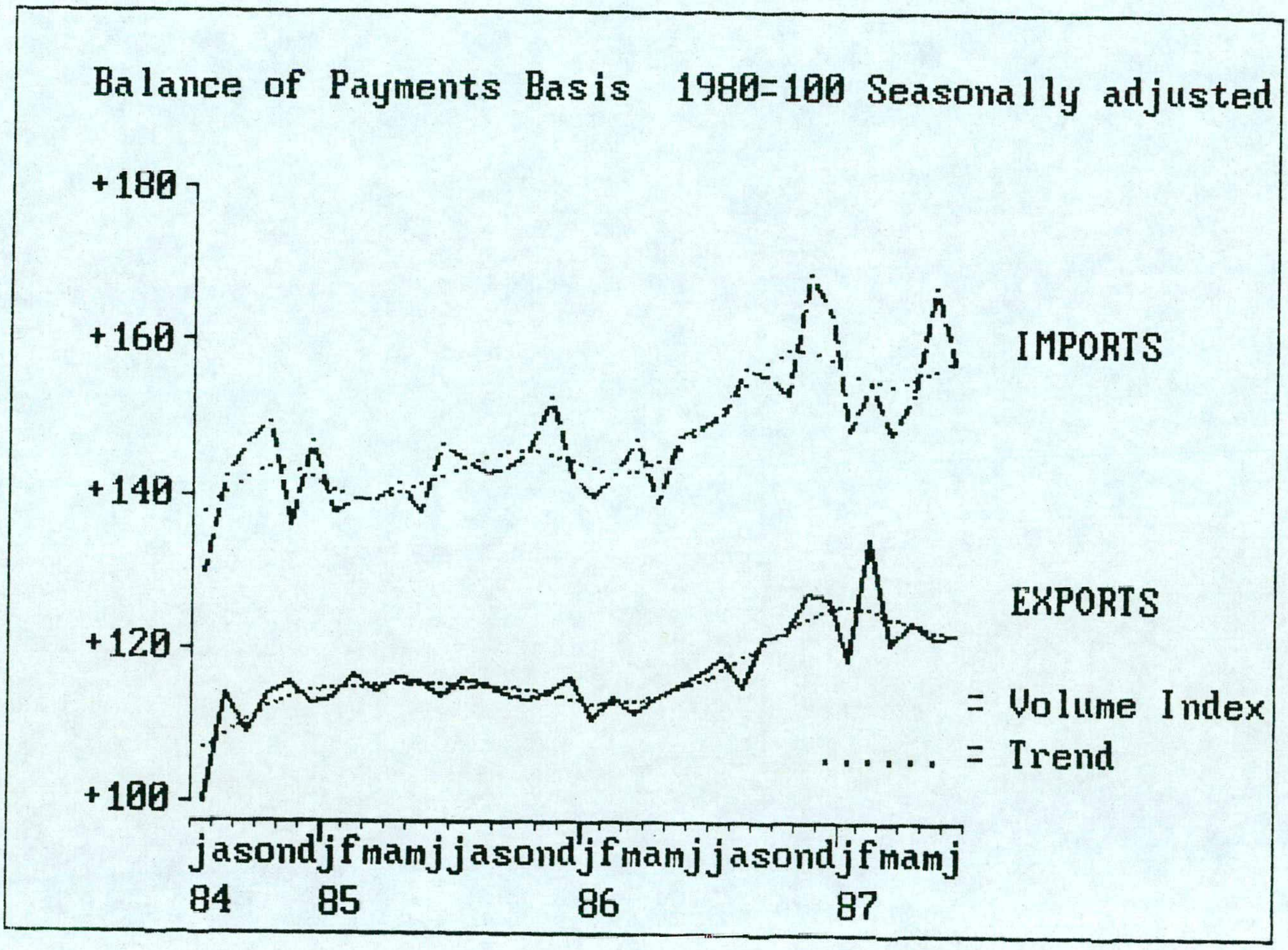
PUBLICATION

The press notice containing the June figures is scheduled for release at 11.30 am on Tuesday 11 August. An announcement about the release date for the July figures will be made at the same time. Our provisional schedule is for publication of the July figures on Tuesday 1 September.

W E Boyd

W E BOYD

VOLUME INDICES EXCLUDING OIL AND THE ERRATICS ITEMS



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5	Chancellor of the Duchy of Lancaster	
6	Sir Robert Armstrong (Cabinet Office)	
7	Sir Brian Hayes (Dept of Trade and Industry)	
8	Sir Peter Middleton (H M Treasury)	
9	Govenor of the Bank of England	
10	Chairman of the Board of H M Customs and Excise	
11	Mr J Hibbert (CSO)	
12	Mr Finlinson (H M Customs and Excise)	
13	Mr B Buckingham (CSO)	
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15	Mr Barrell (H M Treasury)	
16	Mr P Sedgwick (H M Treasury)	
17	Mr D Owen (H M Treasury)	
18	Mr A McIntyre (CSO)	
19	Dr P Rice (Dept of Energy)	
20	Mr Bottrill (H M Treasury)	
21	Mr H H Liesner)	
22	Mr P J Stibbard)	
23	Mr W E Boyd)	
24	Mr E J Wright)	Dept of Trade and
25	Mr A R Hewer)	Industry
26	Miss C Siddell)	
27	Miss H Chapman)	
28	Mr D Packer)	

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on 11 August 1987 at 11.30am

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5/8.
to Alex

To: Minister for Trade copy No..3..(28)

[Disappointing, but key to market reaction will be import figs.]

From Peter Stibbard
US/S2
V/260 Ext. 4872

31 July 1987

OVERSEAS TRADE FIGURES FOR JUNE 1987: EXPORTS

1 The value of exports in June, seasonally adjusted on a balance of payments basis, is estimated at £6.4 billion, ½ per cent (just £26 million) higher than in May. Exports of both oil and of the erratic items were little changed in June so that excluding these, exports also rose by ½ per cent between May and June.

2 An investigation by Customs and Excise into the effects of industrial action on the processing of import and export entries has resulted in some small revisions to the figures for April and May. These are explained in the attached minute sent yesterday by Customs Statistical Office to the Chancellor of the Exchequer. The figure given above for June incorporates the £72 million mentioned in the minute as the estimated value of unprocessed export documents attributable to the June account.

3 In the second quarter of this year, total export volume was 3 per cent lower than in the previous three months and 3½ per cent higher than in the same period a year earlier. Excluding oil and the erratic items export volume decreased by 1½ per cent between the first and second quarters of this year but stands 6 per cent up on the second quarter of last year. The underlying level of non-oil export volume appears now to have settled at a level a little below that reached at the end of last year.

4 Recent export figures are shown in the attached table; charts plotting the main aggregates are also attached. Import figures for June are not yet available. A note describing imports and the current account will be circulated on Wednesday 5 August and the press notice is scheduled for release on Tuesday 11 August.

PJS

P J STIBBARD

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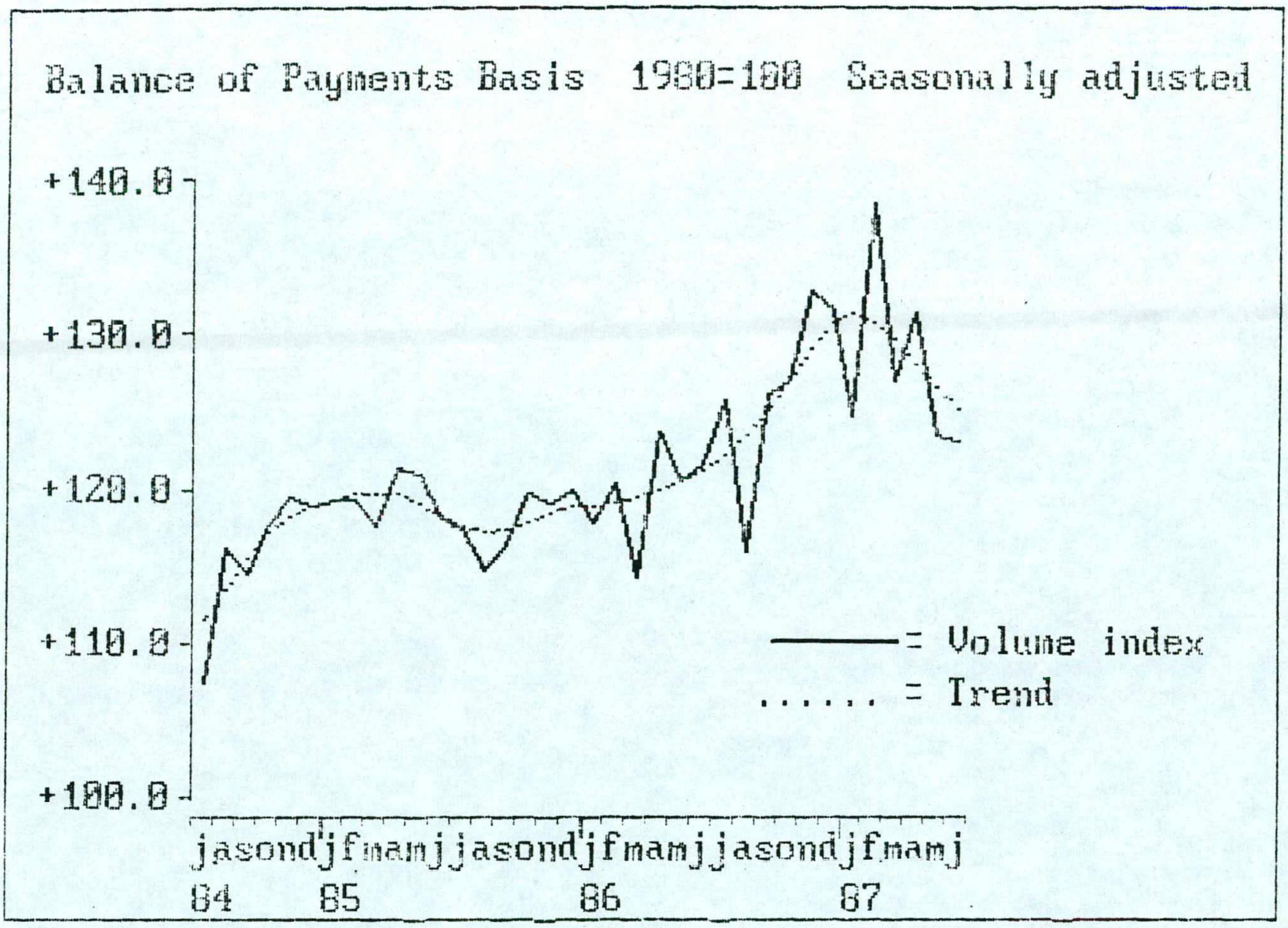
EXPORTS

(Balance of payments basis: seasonally adjusted)

		---TOTAL TRADE---		EXCLUDING --OIL & ERRATICS--	
		VALUE £m	VOLUME (1980=100)	VALUE £m	VOLUME (1980=100)
1986	Q2	17786	121.9	14455	115.1
	Q3	17553	122.6	14839	118.5
	Q4	19340	130.5	15873	125.3
1987	Q1	19637	130.0	15899	124.4
	Q2	19323	126.0	15864	122.3
1987	JAN	6235	124.6	5034	118.7
	FEB	6973	138.4	5697	134.2
	MAR	6429	126.9	5168	120.5
	APR	6604	131.4	5304	123.5
	MAY	6347	123.5	5264	121.4
	JUN	6373	123.1	5296	122.0

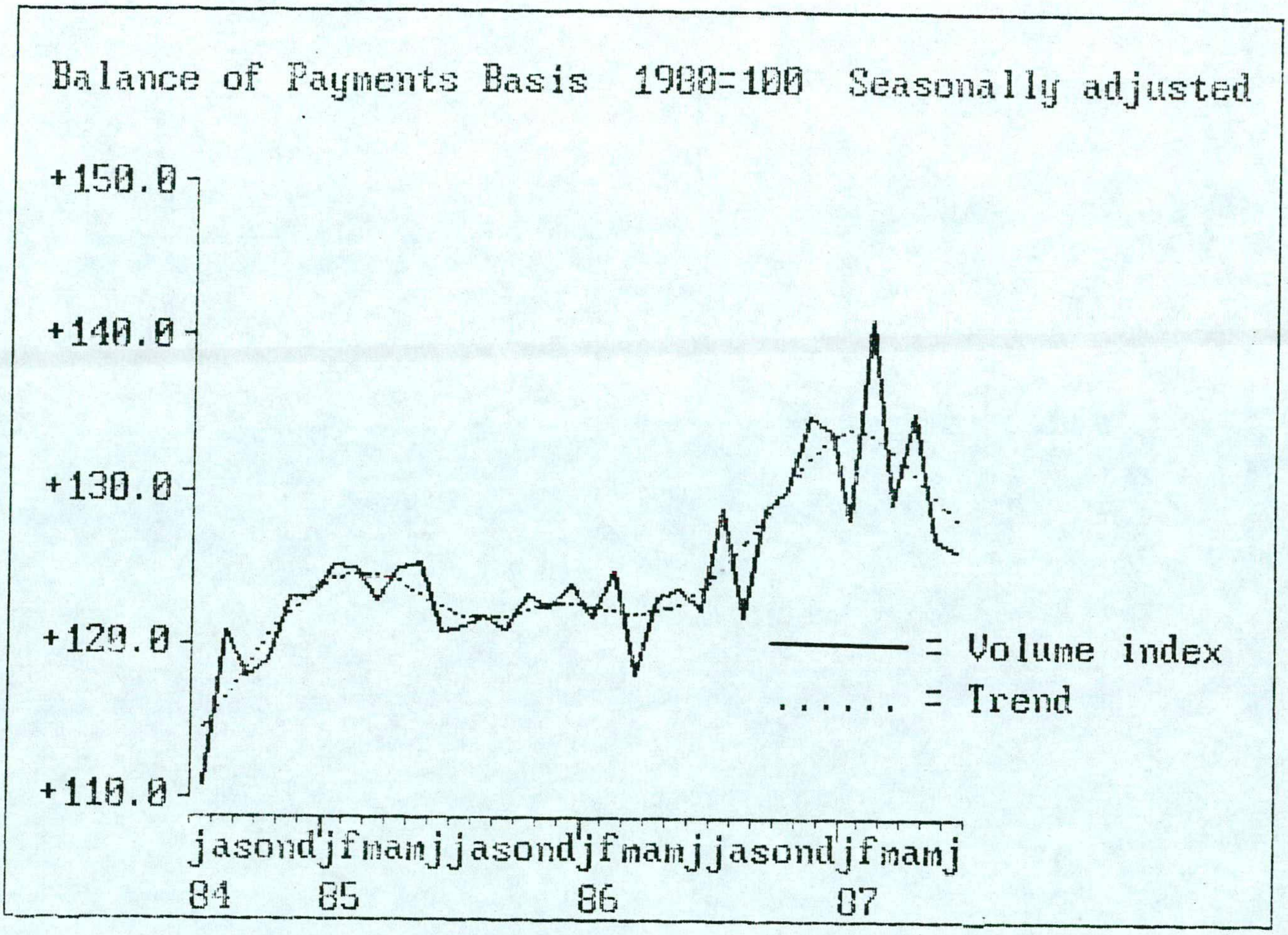
TOTAL EXPORTS



SECRET AND PERSONAL UNTIL RELEASE OF PRESS NOTICE ON 11.8.87

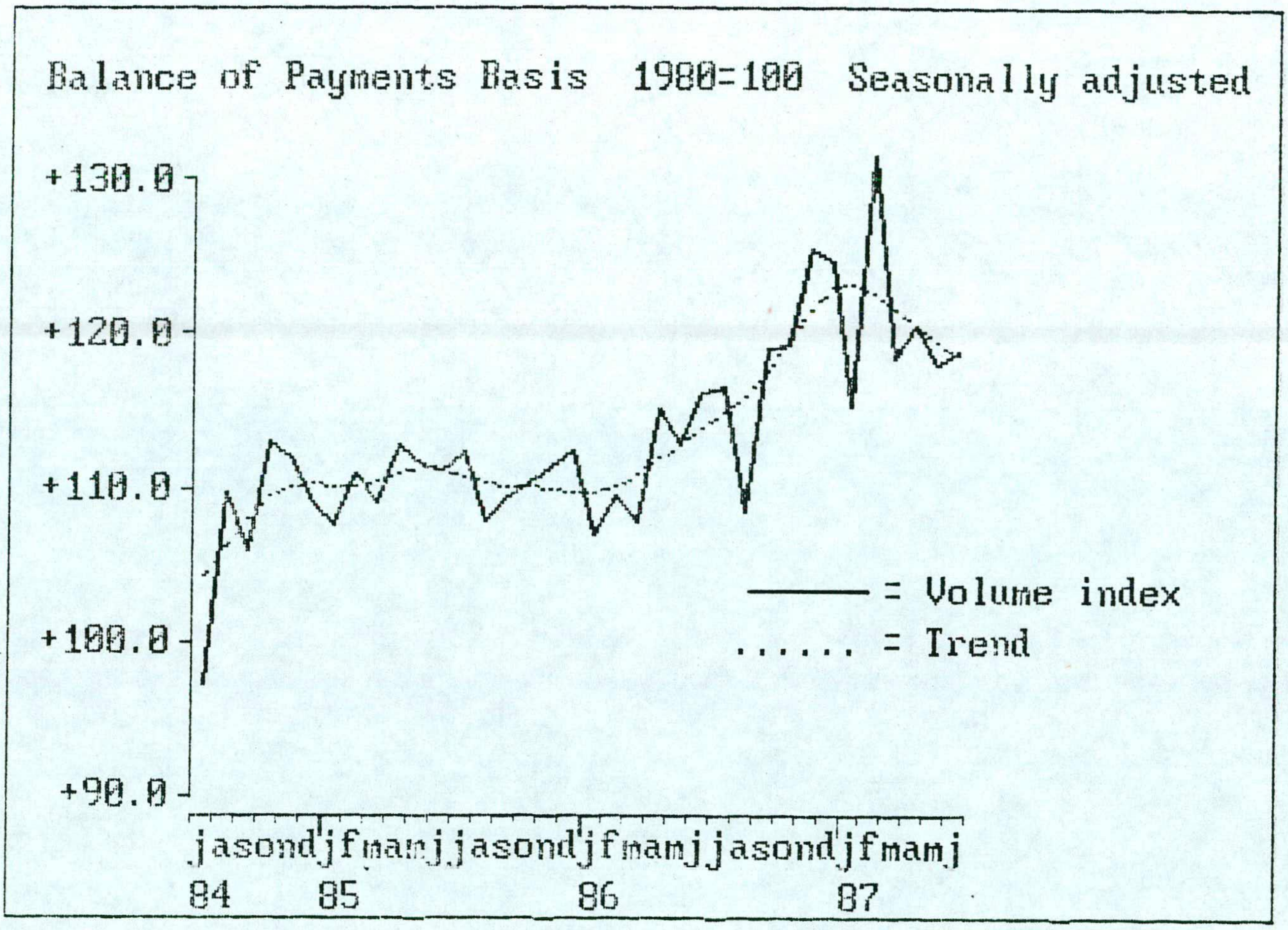
SECRET AND PERSONAL UNTIL RELEASE OF PRESS NOTICE ON 11.8.87

EXPORTS LESS ERRATICS *



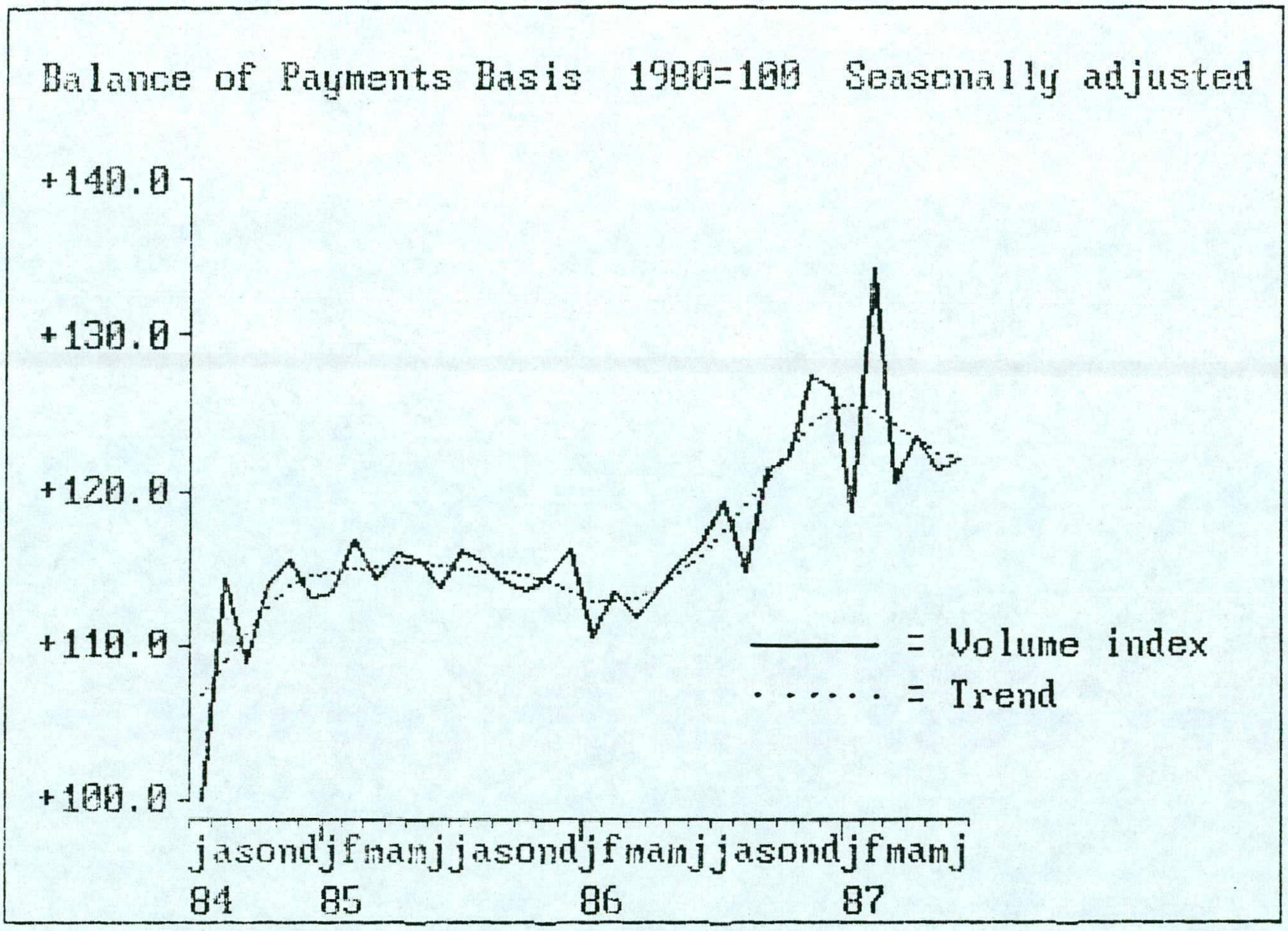
* = Ships, North Sea Rigs, Aircraft, Precious Stones & Silver

EXPORTS LESS OIL



SECRET AND PERSONAL UNTIL RELEASE OF PRESS NOTICE ON 11.8.87

EXPORTS LESS OIL AND ERRATICS



SECRET AND PERSONAL UNTIL RELEASE OF PRESS NOTICE ON 11.8.87

CIRCULATION LIST

Copy No 1 Minister for Trade

2 Prime Minister

3 Chancellor of the Exchequer

4 Secretary of State for Trade and Industry

5 Chancellor of the Duchy of Lancaster

6 Sir Robert Armstrong (Cabinet Office)

7 Sir Brian Hayes (Dept of Trade and Industry)

8 Sir Peter Middleton (H M Treasury)

9 Govenor of the Bank of England

10 Chairman of the Board of H M Customs and Excise

11 Mr J Hibbert (CSO)

12 Mr Finlinson (H M Customs and Excise)

13 Mr B Buckingham (CSO)

14 Mr Davies (H M Treasury)

15 Mr Barrell (H M Treasury)

16 Mr P Sedgwick (H M Treasury)

17 Mr D Owen (H M Treasury)

18 Mr A McIntyre (CSO)

19 Dr P Rice (Dept of Energy)

20 Mr Bottrill (H M Treasury)

21 Mr H H Liesner)

22 Mr P J Stibbard)

23 Mr W E Boyd)

24 Mr E J Wright) Dept of Trade and

25 Mr A R Hewer) Industry

26 Miss C Siddell)

27 Miss H Chapman)

28 Mr D Packer)

H. M. CUSTOMS AND EXCISE
STATISTICAL OFFICE
PORTCULLIS HOUSE, 27 VICTORIA AVENUE, SOUTHEND ON SEA
ESSEX SS2 6AL
TELEPHONE: 0702 36 7155

CONFIDENTIAL

FROM: C C FINLINSON
DATE: 30 July 1987

CHANCELLOR OF THE EXCHEQUER

cc PS/Chief Secretary
PS/Paymaster General
Sir Peter Middleton
Mr Bottrill
Mr Cropper
Mr Tyrie
Mr Hibbert - CSO
Mr Liesner - DTI
Mr Stibbard - DTI
Mr Boyd - DTI ✓

OVERSEAS TRADE STATISTICS

You will wish to know that we have made detailed enquiries at all locations where there was industrial action in April, May or June which might have affected the processing of import or export entries, and thus affected the capture of data for trade statistics purposes. The result of those enquiries, which we must emphasise are still only estimates with a margin of error of perhaps some 20%, can be summarised as follows.

Internal Distribution: CPS
Mr Knox
Mr Nash
Mr Weston
Mr Harris

SO 100/SM/87
SO 100/21
SO 104/25

	April Account	May Account	(£m)
Understatement of Export Values	32	57	
Understatement of Import Values	64	23	
Net Balance	-32	34	

Although not available at the time the figures above reinforce the statement in the briefing note for May from DTI officials of 16 July following Customs and Excise advice that industrial action at the ports and at our computer centre had a minimal effect on the figures for May.

For the June and July trade statistics accounts we estimate, with the same level of accuracy, that the figures we shall supply to DTI will be understated as follows.

	June Account	July Account	(£m)
Understatement of Export Values	72	47	
Understatement of Import Values	35	—	
Net Balance	37	47	

Within the next 24 hours you will receive a copy of the usual monthly briefing note concerning exports for June 1987 prepared by DTI officials. The figures in that briefing will include a special allowance for the value of exports not included in the detailed Customs statistics for June. The adjustment and also one for imports will be included in the joint DTI/CSO press notice to be published on 11 August. In addition the figures of imports and exports for April and May will be revised in that press notice and the reasons for the revisions will be explained.

Corresponding adjustments, but only affecting exports, will be made in the briefing and press notice on the July figures. The July figures are currently scheduled to be published in the week commencing 31 August.

We are not yet able to give a confident prediction of when the missing import and export data will be brought to account, but as soon as we are able to do so we will confirm the actual values and provide the appropriate briefing. When this information is available DTI will be able to refine the first estimates of the adjustments needed to the April, May, June and July trade figures. When the missing data is fully processed it will be reflected in the very detailed figures published in the "Overseas Trade Statistics of the United Kingdom" for the month in which the data is processed and in the cumulative year to date figures. The DTI will make an off setting adjustment to the figures which we supply to them for that month.

Colin C Finlinson

C C FINLINSON

CONFIDENTIAL

FROM: S P WILLIS
DATE: 3 August 1987

1. MISS PEIRSON
2. CHANCELLOR

cc Chief Secretary
Paymaster General
Sir P Middleton
Mr F E R Butler
Mr Anson
Mr Kemp
Mr Monck
Mr Burgner
Dr Freeman
Mr Luce
Mr Turnbull
Mr Beard
Mr Truman
Mr Tyrie

Ch: Content for me to send an acknowledgement (X below)?

3/8

OK.

OPERATIONAL STRATEGY: USE OF CONSULTANTS

In his letter of 28 July Mr Moore reports briefly on the reaction of the staff and unions to the large scale deployment of consultants on the Local Office Project, to which you agreed in your letter of 10 July. He goes on to report on another matter which is causing industrial unrest in the Department. There is nothing in Mr Moore's approach to this second issue to which we would wish to object and this submission recommends that only an acknowledgement is sent from your Private Office.

X

The LOP Project

2. The first batch of consultants has now arrived and DHSS are pushing ahead with the redeployment of permanent staff to other duties. So far the unions have only protested forcefully at the move; there has been no industrial action. This is satisfactory and you need do no more than note the position.

Limited Period Appointments

3. The conversion of existing case papers from the old to the new style benefits under the Reforms is a major, but one-off, task. The conversion could not be handled entirely by existing staff but the recruitment of more permanent staff would not have been appropriate given its short timescale and the need to reduce manpower in line with the savings the Reforms produce after the initial period of change. The decision was therefore taken to recruit a number of extra staff, but only for the limited duration of the conversion exercise: limited period appointees. This was agreed with us and the necessary financial provision was made.

4. The trade unions, however, are strongly opposed to the use of period appointments. In principle, they accept that such appointments should be made in exceptional circumstances - eg a short-term post or a post which requires expertise unavailable

within the Service. In practice, they always press for the smallest competition to be preceded by an interdepartmental trawl, and see any large scale period appointment recruitment as a threat to job security and career prospects. The DHSS recruitment is on a very much larger scale than previous period appointments and at a more junior level. The unions have responded, after rejecting the DHSS case for such recruitment, by taking industrial action.

5. The industrial action has largely taken the form of two and sometimes more permanent staff being called out on strike for a week for every limited period appointee who has taken up post. The following week a different pair of full-time staff will go on strike, and so on. A few offices have been affected either by indefinite all-out strikes or one day walk-outs. Although some 11,000 man days have so far been lost, the action has affected only up to 40 out of 200 offices to which LPAs are to be posted; currently, only 21 offices are affected. Since LPAs have not been recruited there, London regions have not been affected; and the problems have only been marginal in Scotland. But, although the number of offices affected has been relatively few, we understand that the action has a serious impact and has largely negated the benefits to be expected from the LPA scheme.

6. The line Mr Moore now proposes to take - to remind staff of their obligation to work normally and to warn them that they would not be paid while at home - seems to us to be sensible. Mr Moore does not seek your specific agreement to the course he proposes to take: rather, he writes to inform. In the circumstances, probably not much more than an acknowledgement is required but we suggest that while you might endorse the line being taken by the Secretary of State over the LPA question, a reminder should be included as to the Treasury's continuing interest in the wider industrial relations aspects. We suggest that your Private Secretary might write in suitable terms on your behalf. A draft is attached.

7. The issue has been discussed with officials in MPO who have a general responsibility for Limited Period Appointments.

8. IRD agree.

SW.

S P WILLIS
ST2

Psc type / sig

CONFIDENTIAL

DRAFT LETTER FOR PRIVATE SECRETARY SIGNATURE

G J F Podger Esq
Principal Private Secretary to the
Secretary of State for Social Services
Alexander Fleming House
Elephant and Castle
LONDON SE1 6BY

OPERATIONAL STRATEGY: USE OF CONSULTANTS

The Chancellor was grateful for your Secretary of State's further letter of 28 July.

The Local Office Project

2. The Chancellor has noted the reaction of the unions to the wider deployment of consultants on this project.

Limited Period Appointments

3. He has also noted the industrial action taken in opposition to the employment of extra staff for limited periods to handle the implementation of the Social Security Reforms. ~~and~~ He endorses the line your Secretary of State proposes to take for the future.

The Chancellor has asked that your officials keep in close touch with the Treasury on both questions, especially where Service-wide interests and agreements may be concerned.

A copy of this letter goes to the private secretaries to the Prime Minister, the Secretary of State for Employment and Sir Robert Armstrong.

JMG T

Private Secretary

CONFIDENTIAL

FROM: J P MCINTYRE

DATE: 4 August 1987

CHIEF SECRETARY

cc Chancellor
Sir P Middleton
Mr F E R Butler
Miss Peirson
Mr Turnbull
Miss Evans
Mr Gibson
Mr R Watts
Mr Tyrie

Ch
(As I mentioned)
AA

SURVEY: TIMETABLE FOR SOCIAL SECURITY

It would be helpful to have your guidance before the holiday on the line we should take with DHSS officials about the timing of the announcement of the new benefit rates (and also pensions) in the Autumn. Left to themselves, DHSS will probably plan on an announcement very quickly after Parliament returns on 21 October. We would like to tell them to make no assumption about the precise timing just yet because there may be good reasons for having it a little later, and possibly at the time of the Autumn Statement. This recommendation has been discussed with Mr F E R Butler.

Precedents

2. Delaying the uprating announcement until Autumn Statement time was considered last year when, for the first time, the September RPI was the basis for the decisions. The Chancellor and the then Secretary of State decided against delay, and the announcement was on 22 October (the day after the Commons reassembled and five days after publication of the September RPI on 17 October).

The CST will be familiar with this issue. I can see no case for holding up announcement of pledged benefits until the AS. When we do so, there would be a huge Parly row, with suspicions that we were ~~about to~~ reneging on our pledges and - as with last year - hopes that we would announce an uprating in excess of the RPI. We would then be pressed. I do see a case for holding up announcement of the unpledged benefits uprating. Indeed, if we are still arguing about these we would have to ...

3. Other recent upratings announcements were not complicated by the Survey negotiations because they were made in June each year, following publication of the May RPI. The upratings statements in June 1984 and 1985 were each made to Parliament within a few days of the RPI announcement, as was the announcement in February 1986, which paved the way for the switch to a September RPI basis.

4. One of the factors influencing the decision to go for a quick announcement last Autumn was concern that delay might result in pressure building up for some upratings more generous than RPI and might also provide DHSS with an opportunity to argue for reversal of savings decisions.

<u>This year's timetable</u>

5. This year, we have two other factors to take into account:

(a) the September RPI will come out rather earlier, on 9 October;

(b) there is likely to be particular interest in the upratings announcement because we will be setting the new benefit rates for the first time.

6. These considerations would probably lead DHSS to opt for an upratings announcement as soon as Parliament returns on 21 October or perhaps the day after, as last year. Further delay would incur extra administrative costs (maybe £1-2 million a week), and an early announcement would no doubt be helpful to them in preparing for the change-over to the new benefit system on 1 April.

7. An early announcement might also be in the Treasury's best interests. The welfare lobbies will be expecting an early statement, following the pattern of previous years. Knowing the September RPI and equipped with the illustrative rates for the new benefits given in the White Paper Technical Annex, they will be able to work out what the revalued rates would be. While delaying

a statement until Parliament returns might be reasonably defended, without causing too much fuss, further delay could trigger press speculation about cuts and Treasury/DHSS disagreements; the Opposition may demand a statement. This would be an unhelpful background against which to press our case in Star Chamber and Cabinet for major savings (though it could also make a decision to go for no more than revaluation more attractive in presentational terms and thus help us to resist any DHSS arguments for real increases in rates).

8. However, the Survey timetable does not make an early announcement easy. Star Chamber will not begin until 12 October. This would leave only 10 days or so for agreement to be reached on the new rates if Mr Moore were to make his statement on Parliament's return. It is not clear that we could get Star Chamber and the Prime Minister to make difficult decisions within this timescale, ahead of decisions on other Departments. (We could aim to make the timetable less demanding by focusing only on rates in the early stage of Star Chamber, leaving our other savings options for further discussion. But it would be hard to get two bites at the cherry, especially if there were a hostile reception to the rates announcement, and we do not recommend this strategy).

9. There might, in any case, be an argument for trying to establish the principle that the upratings announcement is made at Autumn Statement time, along with other major public expenditure decisions. This year, that would mean a gap of 4-6 weeks from the RPI announcement of 9 October to the Autumn Statement. (Miss Evans' minute to the Chancellor of 31 July discussed the possible timing of the Autumn Statement).

Conclusion

10. We are not sure at this stage whether it would be in the Treasury's interests to go for an early announcement on Social Security. We may want to take a little longer than has been the practice, possibly till Autumn Statement time. If you agree, we will tell DHSS officials that options should be kept open for the time being.

11. If, however, DHSS react adversely to this line, we may need to ask you to write to Mr Moore.

JM

J P MCINTYRE

3761/005

CONFIDENTIAL

Papers please

FROM: G R WESTHEAD
DATE: 5 August 1987

PWP

PS/CHANCELLOR

cc Sir P Middleton
Sir T Burns
Sir G Littler
Mr Cassell
Mr Sedgwick
Mr Culpin
Mr Peretz
Mr C W Kelly
Miss Noble
Mr Pike
Mr Richardson
Mr P S Hall

Ch/ Mr Maude has now agreed to publication in this form.

OK

JF 7/8

DTI PRESS NOTICE ON CONSUMER CREDIT : EXPANDED COVERAGE

The Economic Secretary has considered this further with Mr Peretz after today learning of the June trade figures.

2. The Economic Secretary has concluded that given that the expanded figures will not actually incorporate any real new news - the bank lending figures already being in the public domain - we do not have strong enough grounds for trying to persuade DTI Ministers to delay changing the format for these figures until November; or indeed to delay the 10 August publication date to which DTI are already publically committed (albeit not to publishing the figures in expanded form). He accepts, nevertheless, that this could give the press a few more figures to use in their stories.

3. In answer to the Chancellor's query, noted in Mr Kuczys' minute of 31 July, Mr Peretz pointed out that regardless of their value or otherwise as an economic indicator, DTI would argue that they have a statutory responsibility under the Consumer Credit Act to monitor consumer lending. DTI, and their Ministers, had concluded that the statistics should be expanded, because they were incomplete without incorporating details of bank lending.

Guy Westhead.

GUY WESTHEAD
Assistant Private Secretary

ps3/63K

CONFIDENTIAL

PMP

FROM: A W KUCZYS
DATE: 31 July 1987

PS/ECONOMIC SECRETARY

cc Sir P Middleton
Sir T Burns
Sir G Littler
Mr Cassell
Mr Sedgwick
Mr Peretz
Mrs Lomax
Mr Culpin
Mr C W Kelly
Miss Noble
Mr Pickford
Mr Grice

DTI PRESS NOTICE ON CONSUMER CREDIT: EXPANDED COVERAGE

The Chancellor has seen Mr Grice's minute of 29 July. He was always under the impression that the consumer credit series was pretty worthless as an economic indicator. Is this so? If so, why give it a higher profile?

AWK

A W KUCZYS

4560/028

CONFIDENTIAL until 11.8.87
THEN
UNCLASSIFIED

FROM: J W GRICE
DATE: 29 July 1987

ECONOMIC SECRETARY

cc Chancellor
Sir P Middleton
Sir T Burns
Sir G Littler
Mr Cassell
Mr Sedgwick
Mr Peretz
Mrs Lomax
Mr Culpin
Mr C W Kelly
Miss Noble
Mr Pickford
Mr Pike
Mr Richardson
Mr Allum
Mr P S Hall
Mr Brook

Ch/ Are you content (para 6), subject to Ohr keeping a firm eye on the briefing?
30/7

DTI PRESS NOTICE ON CONSUMER CREDIT: EXPANDED COVERAGE

The Department of Trade and Industry publish each month a Press Notice on consumer credit within the ambit of the 1974 Consumer Credit Act. In the last few days, we have been told informally that a significant change in the coverage of the Press Notice is planned. DTI statisticians will be submitting to their own Ministers within the next few days and the submission will be copied to you. The present submission is intended to warn you in advance and to provide some background.

below

2. We were initially worried that this could give the consumer credit figures a higher profile than hitherto, and create potential presentational problems. But having discussed this with DTI we are now content that we can handle any minor presentational difficulties that might arise with what is proposed.

The Background

3. To date, the DTI monthly Press Notice has not given figures on bank lending to consumers because the information has not been available. But in future, on a quarterly basis, it will contain

data on bank loans to the personal sector of less than £15,000 and such loans will be deemed to be consumer credit. (There is already a table in <u>Financial Statistics</u> where bank lending to households other than for house purchase is treated as consumer credit. But this table - from which the consumer credit statistics in the Chancellor's FHA speech were derived - is not very timely and has not attracted press interest in the past.) Attached is a mock-up of what the Press Notice will look like on the new basis (the figures are not reliable at this stage).

4. After we were told of the intended change, we discussed the matter with DTI, the Bank of England and the CSO. The following were the main points to emerge:

i. the extended Press Notice should contain relatively little news so far as the market is concerned. The new data, on which any interest is likely to focus, will be only quarterly. The next publication date is 10 August and will give the position as at the end of June. By that stage, the full June money figures will already have been published. Whilst the Press Notice will give the first official figures on bank lending to consumers, the market will already have some idea of the sectoral split of bank lending from the monthly data published by the Committee of London and Scottish Banks (CLSB). The Bank of England see no difficulty on this score;

ii. DTI accept that consumer credit figures are currently sensitive and will normally restrict the text of the Press Notice to a verbal description of the figures. We have pressed DTI hard to give us the opportunity to comment on the Press Notice and associated briefing in draft form. That seems to be logistically impossible on this first occasion. DTI are committed to publishing the Press Notice on Monday 10 August at 11.30 am but the data will not be available to enable the Notice to be produced until lunch time on Friday 7 August, leaving no time for us to comment. But they have agreed to consider with us the possibility of adding an extra 24 hours to the timetable for the future so that Treasury Ministers will have an opportunity to comment. In fact, because the new sensitive data will be updated only quarterly, the next occasion will not arise until the Press Notice for publication in November;

iii. DTI Press Office will deal with detailed queries on the figures but will refer, as now, questions on monetary or credit policy to the Treasury Press Office.

Action

4. No action is required if you are content to let DTI proceed as they currently intend. We have given thought as to whether DTI should be asked not to proceed in view of the current sensitivity of this area. On balance, we recommend against this course. DTI have a good case for wanting to publish these fuller figures. They have a statutory obligation to monitor consumer lending under the 1974 Act. Moreover the figures will only be published quarterly, some time in arrears, and well after the relevant monthly money and clearing bank lending figures. There is also something to be said for the first such figure being published in August. But we will, of course, need to keep a firm watch on DTI's briefing, and make sure that any questions on monetary policy are referred to the Treasury.

JWG

J W GRICE

DRAFT 1A

CREDIT BUSINESS IN JUNE

During June the change in amounts outstanding on consumer credit agreements with finance houses, other specialist credit grantors, building societies, retailers and on bank credit cards was £0.3 billion (see table 1). This was equal to the increase in May.

The increase in the latest three months, April to June, was £1.0 billion, the same as in the previous three months. Within the total, the increase shown by finance houses, other specialist credit grantors and building societies was £0.8 billion in the most recent period compared to £0.6 billion in the previous one. Bank credit cards showed an increase of £0.2 billion in both three month periods. Retailers also showed similar increases, of £0.1 billion.

[Bank loans on personal accounts showed an increase in amounts outstanding of £0.5 billion, lower than the previous quarter's value of £0.7 billion (see table 1A). Including these loans and loans by insurance companies, figures for which are available only quarterly, gives a total increase in consumer credit in the April to June quarter of £1.5 billion, down from £1.7 billion in the preceding quarter.]

[At the end of the quarter, the total amount outstanding on consumer credit agreements was £34.2 billion, 5 per cent more than the total at the end of the previous quarter.]

New credit advanced to consumers in June by finance houses, other specialist credit grantors, building societies, retailers and on bank credit cards amounted to £2.7 billion, a similar total to that in May (see table 2). The total for the three months April to June was 3 per cent higher than that for the previous three months.

In June there was a **change in amounts outstanding on agreements with businesses** by finance houses and other specialist credit grantors of £0.1 billion (see table 1). The total change in the latest three months was £0.3 billion compared to no change in the preceding three months. [At the end of June the total value of the outstanding amounts was £6.1 billion.]

N.B. [ ] indicate passages to be included in press notices for March, June, September and December but not for other months.

FINANCE HOUSES, OTHER SPECIALIST CREDIT GRANTORS AND BUILDING SOCIETIES, RETAILERS AND ON BANK CREDIT CARDS. (SEASONALLY ADJUSTE

£ Million

	AGREEMENTS WITH CONSUMERS				AGREEMENTS WITH BUSINESSES	TOTAL AGREEMENTS
	TOTAL	RETAILERS (a)	BANK CREDIT CARDS	FINANCE HOUSES, OTHER SPECIALIST CREDIT GRANTORS AND BUILDING SOCIETIES ON AGREEMENTS WITH		
				CONSUMERS	BUSINESSES	
AMOUNT OUTSTANDING AT END OF PERIOD						
1986	19,063	2,231	4,681	12,151	5,728	24,791
1987 JUNE	21,018	2,358	5,081	13,579	6,060	27,078
CHANGES IN AMOUNTS OUTSTANDING						
1986	2,365	94	819	1,452	596	2,961
1986 1st Qtr	855	39	221	595	214	1,069
2nd Qtr	346	3	213	130	34	380
3rd Qtr	792	107	356	329	193	985
4th Qtr	444	-55	101	398	155	599
1987 1st Qtr	952	67	248	637	5	957
2nd Qtr	1,003	60	152	791	327	1,330
1986 JUN	167	9	109	49	21	188
JUL	183	28	80	75	73	256
AUG	217	34	82	101	48	265
SEP	392	45	194	153	72	545
OCT	194	-81	86	189	127	321
NOV	-15	12	-113	86	-23	-38
DEC	265	14	128	123	51	316
1987 JAN	257	8	15	234	-17	240
FEB	296	27	97	172	24	320
MAR	399	32	136	231	-2	397
APR	410	20	113	277	66	476
MAY	303	20	19	264	141	444
JUN	290	20	20	250	120	410
1987 JAN-MAR	952	67	248	637	5	957
1987 APR-JUN	1,003	60	152	791	327	1,330

R = revised

TES (a) Self-financed advances by clothing retailers, household goods retailers mixed retail businesses (other than Co-operative societies) and general mail order houses only.

(b) Data were not collected on a consistent basis for all types of credit grantor prior to 1986. The following table gives figures for changes in amounts outstanding which are available:

£ Million

	1983	1984	1985
Retailers	132	116	195
Finance houses etc	2,286	2,180	2,541

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TABLE 1A

CHANGES IN AMOUNTS OUTSTANDING TO FINANCE HOUSES, OTHER SPECIALIST CREDIT GRANTORS AND BUILDING SOCIETIES, RETAILERS, BANKS ON CREDIT CARDS AND PERSONAL ACCOUNTS AND TO INSURANCE COMPANIES ON CONSUMER LOANS. (SEASONALLY ADJUSTED)

£ Million

	AGREEMENTS WITH CONSUMERS						AGREEMENTS WITH BUSINESSES	TOTAL AGREEMENTS (a)
			BANKS (c)			FINANCE HOUSES, OTHER SPECIALIST CREDIT GRANTORS AND BUILDING SOCIETIES ON AGREEMENTS WITH		
	TOTAL (a)	RETAILERS (b)	CREDIT CARDS	LOANS ON PERSONAL ACCOUNTS (d)	INSURANCE COMPANIES	CONSUMERS	BUSINESSES	
AMOUNT OUTSTANDING AT END OF PERIOD								
1986	30,996	2,231	4,681	11,129	804	12,151	5,728	36,724
1987 2nd Qtr	34,240	2,358	5,081	12,400	822	13,579	6,060	40,300
CHANGES IN AMOUNTS OUTSTANDING (d)								
1986	2,496	94	819		59	1,452	596	3,092
1986 1st Qtr	857	39	221		3	595	214	1,071
2nd Qtr	360	3	213		14	130	34	394
3rd Qtr	806	107	356		14	329	193	999
4th Qtr	472	-55	101		28	398	155	627
1987 1st Qtr	1,739	67	248	779	8	637	5	1,744
2nd Qtr	1,505	60	152	492	10	791	327	1,832

—— indicates a break in the series

R = revised

NOTES

(a) Changes in amounts outstanding in 1986 exclude bank loans on personal accounts.

(b) Self-financed advances by clothing retailers, household goods retailers mixed retail businesses (other than Co-operative societies) and general mail order houses only.

(c) Monetary sector institutions other than those included in finance houses and other specialist credit grantors.

(d) Amounts outstanding on bank loans on personal accounts, not exceeding £15,000, excluding bridging loans and house purchase finance.

PB P

To Mr Maude

From Peter Stibbard
US/S2
V/260 Ext. 4872

30 July 1987

cc Secretary of State
Mr Clarke, CDL
Mr Butcher
Chancellor of the Exchequer
Economic Secretary

Sir Brian Hayes
Mr Liesner
Mr Harvey S1
Mr Newton CA
Mr Ward BSO
Mr Whiting Ec2
Mr Moorey Inf
Mr Richardson S2C
Miss Marson S2C
Ms Partridge Inf
Mr Thomas OFT

Mr Flemming Bank of England
Mr Bull "
Mr Wells CSO
Mr Alexander CSO
Mr Cassell Treasury
Mr Pike Treasury

DTI PRESS NOTICE ON CREDIT BUSINESS STATISTICS

The Issue

1 This submission gives advance notice of changes to the monthly DTI statistical press notice on credit business, starting with the press notice for June, to be issued on Monday, 10 August. These affect both the coverage and the presentation of the statistics. The main change in coverage is the inclusion of quarterly figures on bank personal loans and overdrafts on personal accounts; and the change in presentation is that we are now giving the main emphasis to 'changes in amounts outstanding' rather than 'new credit advanced'.

Recommendation

2 I recommend that these changes, which have been discussed and agreed with officials from the Treasury and the Bank of England, the Central Statistical Office, and with DTI Information Division, should be made.

Timing

3 The next press notice on credit business statistics is to be issued on Monday, 10 August. This date has been included in the

list of release dates of economic statistics published by the Central Statistical Office. (As usual, it coincides with publication of the DTI press notice giving final monthly retail sales figures - provisional figures are released about three weeks earlier). To be able to take account of any comments on the format of the press notice we would like to receive them by this coming Monday, 3 August.

Background

4 Statistics on credit business are collected by this Department because of its role in monitoring the effects of the Consumer Credit Act 1974. Monthly data have been collected from finance houses and other specialist credit grantors and from retailers for many years, and published by press notice. The continuation of the statistical inquiries to the former group was approved by Mr Butcher following a detailed review which I submitted on 13 December 1985. (The inquiry to retailers forms part of the monthly Retail Sales Inquiry, the review of which was approved by Mr Butcher on 5 July 1985).

5 As the coverage of the Consumer Credit Act has been extended we have expanded the coverage of our statistics published in the press notice. Data on bank credit cards, obtained from the Committee of London and Scottish Bankers (CLSB), were included from January 1986. From the start of this year we have incorporated data on building societies' unsecured lending, which have been provided by the Building Societies Association.

6 Also since the beginning of this year we have been collecting quarterly data on bank personal loans, and overdrafts on personal accounts, not exceeding £15,000 (the upper limit of personal loans to individuals regulated under the Consumer Credit Act). We are now ready to publish this information, as promised to the CLSB when we started to collect it. This is the main change to the coverage of the press notice. [We had hoped to be able to obtain these data from either the CLSB or the Bank of England - as envisaged in my submission to Mr Butcher of 20 January 1986. This did not prove possible in the short-term, although discussions are continuing. Meanwhile we have been collecting quarterly information directly from 11 large banks consisting of two items only; these cover some 90% of the total lending of this type and we have made estimates for the remainder.]

Argument

7 In our statistics we shall now cover all sources of finance for consumers, thus giving a reasonably accurate and comprehensive figure for total consumer credit (defined to exclude the main sources of loans for house purchase). This is an important economic indicator, of wide interest inside and outside Government. Until now the only source for figures of comparable coverage has been the Central Statistical Office. Their total is derived differently and they publish the

figures in their publication Financial Statistics (Table 9.3, a copy of which is attached as Annex A). The CSO figures become available much later eg their data for the quarter ended June 1987 will not be published until the end of October. [The CSO are now reviewing the format of Financial Statistics Table 9.3. They are considering using the new DTI figures in Financial Statistics and discontinuing their own figures of consumer credit - thus preventing the confusion that would be caused by the existence of two official series of broadly similar coverage].

8 As stated above, we propose to include the new statistics on bank personal loans and overdrafts in the tables in the 10 August Press Notice. Figures on total bank lending in June and on lending to the private sector were published on 20 July by the Bank of England in the latest of their regular press notices on money and banking statistics. More detailed figures concerning personal lending were published at the same time by the CLSB. Together, these figures for June excited considerable media interest and affected financial markets. The banking figures we propose to publish will be a (previously indistinguishable) sub-set of those already published on 20 July, supplemented by the latest figures from the other sources of consumer credit covered already by the DTI press notice on credit business.

9 To complete the picture, we also intend to include loans by insurance companies to individuals in our press notice. These quarterly figures are available from inquiries already conducted by this Division for another purpose, but as these are not timely we shall have to make estimates for the latest quarter, and revise the figures later. However, the amounts involved are very small in relation to total consumer credit.

10 Simultaneously we propose to change the presentation of the statistics. Until now the main emphasis of the press notice has been new credit advanced (ie gross lending, excluding repayments). This has included 'turnover' on bank credit cards (Visa and Access) and the importance of bank credit cards in consumer credit has thus been exaggerated to the extent these are used as a method of payment rather than as a means of obtaining credit. We propose to ameliorate this problem by giving main prominence to changes in amounts outstanding. This change also has the advantage of concentrating attention on the series for which we have full coverage (eg we do not - yet - have information on new credit advanced on bank personal loans). We also intend to give more prominence to consumer lending (hitherto lending to businesses by finance houses was included in the main aggregate featured in the press notice).

11 The formats of the three tables we propose to include in the press notice are shown in Annex B. Table 1 presents the changes in amounts outstanding on the items for which we have monthly figures. Table 2 reproduces the data from Table 1 as quarterly totals, supplemented by the new quarterly data on bank personal loans and overdrafts and

insurance company loans that we now wish to publish. Table 3 presents the available monthly data on new credit advanced, which was previously given most prominence in the press notice. Table 2 will not, of course, be updated again until the figures for Q3 are available (apart from revisions to Table 1 carried into Table 2). The Q3 figures will be published in the press notice issued in November. The tables in Annex B do not include any figures for June or Q2 because we are only now receiving this information from the respondents to our surveys. Table 2 has been marked 'confidential' because the Q1 figures for bank loans and overdrafts have not, of course, been published. A rough outline of the text of the press notice is also shown in Annex B.

12 The press notice to be issued on 10 August will include additional notes explaining the increased coverage and the changed presentation. Special briefing on this topic will also be provided to the DTI press office and copied to other relevant Departmental press offices.

13 Also attached, at Annex C, is an information copy of the most recent issue of the DTI credit business press notice in its present form.

14 Finally, Annex D is a chart illustrating the past, present and proposed future coverage of DTI consumer credit statistics, expressed in amounts outstanding. We do not intend to include this chart in the press notice, but we may, if space allows, include something like it in the subsequent monthly article in British Business, as an explanatory aid.

15 An advance information copy of the Press Notice will be sent to Ministers on the afternoon of Friday, 7 August complete with the figures for June and Q2, which will become known during the morning of that day. Special arrangements have been made to telephone the main figures to Treasury officials as soon as they are firm; they have asked to have them to use for internal briefing in the Treasury.

P J STIBBARD

9.3 Consumer credit and other personal sector borrowing

£ million

	Consumer credit: Total		Monetary sector (1)						Other borrowing			
	Unadjusted	Seasonally adjusted	Total	of which: credit card lending	Trustee saving banks	Non-Monetary sector credit companies	Insurance companies	Retailers	Loans for house purchase	Monetary sector	Other	Total borrowing
Amount outstanding at end of period	AILA		AILB	AILI	AILC.	AGRJ	AILE	AILF	AILG	AILH		
1982	16,030		12,602	2,020		1,317	317	1,794	76,325	12,501		
1983	18,932†		14,804	2,592		1,842	356†	1,930	91,430	14,798		
1984	22,348		17,415	3,199		2,204	683	2,046	108,464	16,486		
1985	26,160		20,352	4,052		2,815	745	2,248	127,536†	20,186		
1986	30,685		23,827†			3,758	804	2,296	153,363	19,956†		
Net transactions	AIKL	AIKM	AIKN	AIKP	AIKO	AGSJ	AIKQ	AAPP	AAPR	AIKR	AIKS	AIJP
1982	2,621		2,344			125	19	133	14,123	2,645	147	19,536
1983	3,284		2,583			525	40	136	14,501	2,310	243	20,338
1984	3,094		2,604			362	12	116	17,034	1,577	378	22,083
1985	3,812†		2,937†			611	62	202	19,072†	3,891	762	27,537†
1986	4,477	4,477	3,476			894	59	48	25,827	2,575†	-394†	32,485
1982 1	243	525	316			-38	5	-40	2,693	782	-37	3,681
2	551	515	564			1	5	-19	3,545	810	-265	4,641
3	845	737	772			49	4	20	3,845	813	-141	5,362
4	982	844	692			113	5	172	4,040	240	590	5,852
1983 1	464	776	361			76	4	23	3,629	584	190	4,867
2	849	828	812			68	10	-41	3,707	858	-388	5,026
3	972	829	802			158	11	1	3,580	572	-70	5,054
4	999	851	608			223	15	153	3,585	296	511	5,391
1984 1	438	771	307			163	3	-35	3,512	380	207	4,537
2	988	974	965			94	5	-76	4,733	483	-159	6,045
3	770	604	696			51	3	20	4,591	626	-141	5,846
4	898	745	636			54	1	207	4,198	88	471	5,655
1985 1	506	852	427			77	14	-12	3,683	1,191	524	5,904
2	999	981	836			207	14	-58	4,577	964	-406	6,134
3	1,213†	1,038†	945†			223	17	28	5,320†	801	-227	7,107†
4	1,094	941	729			104	17	244	5,492	935	871	8,392
1986 1	599	948	426			185	3	-15	4,448	911†	244	6,202
2	1,180	1,162	1,125			152	14	-111	6,379	1,715	-730†	8,544
3	1,637	1,458	1,276			260	14	87	7,880	-220	15	9,312
4	1,061	909	649			297	28	87	7,120	169	77	8,427
1987 1			561			180†				1,572		

1. Up to 1981 includes consumer credit companies recognised as banks.
From 1982 includes consumer credit companies licensed to take deposits.

Source: Central Statistical Office.

[Extract from the June 1987 edition of Financial Statistics]

CREDIT BUSINESS IN JUNE

During June the **change in amounts outstanding on consumer credit agreements** with finance houses, other specialist credit grantors, building societies, retailers and on bank credit cards was £[ ] billion (see **Table 1**). [Sentence comparing the June and May figures].

The increase in the latest three months, April to June, was £[ ] billion, [comparison with previous three months]. Within the total, the [decrease/increase] shown by finance houses, other specialist credit grantors and building societies was £[ ] billion in the most recent period compared to £[ ] billion in the previous one. Bank credit cards showed an increase of £[ ] billion. Retailers also showed similar increases, of £[ ] billion in the most recent three month period and £[ ] billion in the previous three month period.

[[Bank loans on personal accounts showed an increase in amounts outstanding of £[ ] billion, [lower/higher] than the previous quarter's value of £[ ] billion (see **Table 2**.) Including these loans and loans to individuals by insurance companies, figures for which are available only quarterly, gives a **total increase in consumer credit** in the April to June quarter of £[ ] billion, [up/down] from £[ ] billion in the preceding quarter.]]

[[At the end of the quarter, the **total amount outstanding on consumer credit agreements** was £[ ] billion, [ ] per cent [less/more] than the total at the end of the previous quarter.]]

New credit advanced to consumers in June by finance houses, other specialist credit grantors, building societies, retailers and on bank credit cards amounted to £[ ] billion, [sentence comparing with May figures] (see **Table 3**). The total for the three months April to June was [ ] per cent [lower/higher] than that for the previous three months.

In June there was a **change in amounts outstanding on agreements with businesses** by finance houses and other specialist credit grantors of £[ ] billion (see **Table 1**). The total change in the latest three months was £[ ] billion compared to [ ] in the preceding three months. At the end of June the total value of the outstanding amounts was £[ ] billion.

NB [[ ]] indicate passages to be included in press notices for March, June, September and December but not for other months.

TABLE 1

CHANGES IN AMOUNTS OUTSTANDING TO FINANCE HOUSES, OTHER SPECIALIST CREDIT GRANTORS AND BUILDING SOCIETIES, RETAILERS AND ON BANK CREDIT CARDS. (SEASONALLY ADJUSTED)

£ Million

	AGREEMENTS WITH CONSUMERS				AGREEMENTS WITH BUSINESSES	TOTAL AGREEMENTS
	TOTAL	RETAILERS (a)	BANK CREDIT CARDS	FINANCE HOUSES, OTHER SPECIALIST CREDIT GRANTORS AND BUILDING SOCIETIES ON AGREEMENTS WITH CONSUMERS	BUSINESSES	
AMOUNTS OUTSTANDING AT END OF PERIOD						
1986	19,063	2,231	4,681	12,151	5,728	24,791
1987 MAY	20,728	2,338	5,061	13,329	5,940	26,668
CHANGES IN AMOUNTS OUTSTANDING						
1986	2,365	94	819	1,452	596	2,961
1986 1st Qtr	855	39	221	595	214	1,069
2nd Qtr	346	3	213	130	34	380
3rd Qtr	792	107	356	329	193	985
4th Qtr	444	-55	101	398	155	599
1987 1st Qtr	952	67	248	637	5	957
1986 JUN	167	9	109	49	21	188
JUL	183	28	80	75	73	256
AUG	217	34	82	101	48	265
SEP	392	45	194	153	72	545
OCT	194	-81	86	189	127	321
NOV	-15	12	-113	86	-23	-38
DEC	265	14	128	123	51	316
1987 JAN	257	8	15	234	-17	240
FEB	296	27	97	172	24	320
MAR	399	32	136	231	-2	397
APR	410	20	113	277	66	476
MAY	303	20	19	264	141	444
1986 DEC-FEB '87	818	49	240	529	58	876
1987 MAR-MAY	1,112	72	268	772	205	1,317

R = revised

NOTES

(a) Self financed credit advanced by clothing retailers, household goods retailers mixed retail businesses (other than Co-operative societies) and general mail-order houses only.

(b) Data were not collected on a consistent basis for all types of credit grantor prior to 1986. The following table gives figures for changes in amounts outstanding which are available:

£ Million

	1983	1984	1985
Retailers	132	116	195
Finance houses etc.	2,286	2,180	2,541

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TABLE 2

CHANGES IN AMOUNTS OUTSTANDING TO FINANCE HOUSES, OTHER SPECIALIST CREDIT GRANTORS AND BUILDING SOCIETIES, RETAILERS, BANKS ON CREDIT CARDS AND PERSONAL ACCOUNTS AND TO INSURANCE COMPANIES ON CONSUMER LOANS.

(SEASONALLY ADJUSTED)

£ Million

	AGREEMENTS WITH CONSUMERS						AGREEMENTS WITH BUSINESSES	TOTAL AGREEMENTS (a)
			BANKS (c)			FINANCE HOUSES, OTHER SPECIALIST CREDIT GRANTORS AND BUILDING SOCIETIES ON AGREEMENTS WITH		
	TOTAL (a)	RETAILERS (b)	CREDIT CARDS	LOANS ON PERSONAL ACCOUNTS (d)	INSURANCE COMPANIES	CONSUMERS	BUSINESSES	
AMOUNT OUTSTANDING AT END OF PERIOD								
1986	30,996	2,231	4,681	11,129	804	12,151	5,728	36,724
1987 1st Qtr	32,735	2,298	4,929	11,908	812	12,788	5,733	38,468
CHANGES IN AMOUNTS OUTSTANDING								
1986	2,496	94	819		59	1,452	596	3,092
1986 1st Qtr	857	39	221		3	595	214	1,071
2nd Qtr	360	3	213		14	130	34	394
3rd Qtr	806	107	356		14	329	193	999
4th Qtr	472	-55	101		28	398	155	627
1987 1st Qtr	1,739	67	248	779	8	637	5	1,744

—— indicates a break in the series

R = revised

NOTES

(a) Changes in amounts outstanding in 1986 exclude bank loans on personal accounts.

(b) Self-financed advances by clothing retailers, household goods retailers mixed retail businesses (other than Co-operative societies) and general mail order houses only.

(c) Monetary sector institutions other than those included in finance houses and other specialist credit grantors.

(d) Amounts outstanding on bank loans on personal accounts, not exeeding £15,000, excluding bridging loans and house purchase finance.

TABLE 3

NEW CREDIT ADVANCED BY FINANCE HOUSES, OTHER SPECIALIST CREDIT GRANTORS AND BUILDING SOCIETIES, RETAILERS AND ON BANK CREDIT CARDS. (SEASONALLY ADJUSTED)

£ Million

	AGREEMENTS WITH CONSUMERS				AGREEMENTS WITH BUSINESSES	TOTAL AGREEMENTS
				FINANCE HOUSES, OTHER SPECIALIST CREDIT GRANTORS AND BUILDING SOCIETIES ON AGREEMENTS WITH		
	TOTAL	RETAILERS (a)	BANK CREDIT CARDS	CONSUMERS	BUSINESSES	
1986	28,026	4,834	12,916	10,276	3,489	31,515
1986 1st Qtr	6,549	1,146	2,926	2,477	826	7,375
2nd Qtr	6,875	1,191	3,115	2,569	864	7,739
3rd Qtr	7,349	1,267	3,395	2,687	874	8,223
4th Qtr	7,253	1,230	3,480	2,543	925	8,178
1987 1st Qtr	7,918	1,241	3,874	2,083	963	8,881
1986 JUN	2,331	402	1,080	849	282	2,613
JUL	2,411	415	1,107	889	274	2,685
AUG	2,383	421	1,068	894	285	2,668
SEP	2,555	431	1,220	904	315	2,870
OCT	2,437	413	1,152	872	322	2,759
NOV	2,360	420	1,129	811	275	2,635
DEC	2,456	397	1,199	860	328	2,784
1987 JAN	2,417	411	1,177	829	278	2,695
FEB	2,618	415	1,276	927	331	2,949
MAR	2,883	415	1,421	1,047	354	3,237
APR	2,766	416	1,289	1,061	314	3,080
MAY	2,708	414	1,268	1,026	335	3,043
1986 DEC-FEB'87	7,491	1,223	3,652	2,616	937	8,428
1987 MAR-MAY	8,357	1,245	3,978	3,134	1,003	9,360
Percentage increase over previous quarter	12	2	9	20	7	11

R = revised

NOTES (a) Self financed credit advanced by clothing retailers, household goods retailers, mixed retail businesses (other than Co-operative societies) and general mail-order houses only.

DTI Press Notice

Department of Trade and Industry
1 Victoria Street SW1H 0ET
Press Office: 01-215 4471/4475
Out of hours: 01-215 7877

No 87/379

6 July 1987

CREDIT BUSINESS IN MAY

During May £3.0 billion of **new credit** was advanced by finance houses, other specialist credit grantors, retailers and on bank credit cards. This was below the levels of the previous two months, the fall being shown by all types of credit grantor.

Total advances in the latest three months, March to May, were 11 per cent higher than in the previous three months. Lending by finance houses and other specialist credit grantors increased by 16 per cent between the two periods. Within this total, lending to consumers increased by 20 per cent and lending to businesses increased by 7 per cent. Advances on bank credit cards increased by 9 per cent between the two periods. Retailers advanced 2 per cent more in the latest three months than in the previous three months.

There was an increase of £0.4 billion in **amounts outstanding** to finance houses, other specialist credit grantors, retailers and on bank credit cards between end-April and end-May. The total amount outstanding at end-May was £25.6 billion, 5 per cent more than the total three months earlier.

Notes to Editors

1 All figures are quoted after seasonal adjustment.

2 Table 1 covers the credit business of finance houses, other specialist credit grantors and building societies, retailers and on bank credit cards. Table 2 covers the business of finance houses, other specialist credit grantors and building societies only, but provides an analysis of new credit advanced to consumers and businesses. The credit advances shown in Table 1 for retailers and bank credit cards are mainly to consumers. A high proportion of credit advances in certain types of agreement, notably on bank credit cards and by mail order houses, is repaid within a month, reflecting the use of such agreements as a method of payment rather than as a means of obtaining credit.

3 From January 1986 the statistics include new credit advances by finance houses and other specialist credit grantors on running account agreements on which information was not collected previously. Lending on bank credit cards is also included for the first time in the January 1986 statistics. Unsecured loans by building societies, which are advanced under the provisions of the Building Societies Act 1986, are included from January 1987. Lending by banks, other than on bank credit cards, and by companies where the group specialises in lending to other companies only are excluded from the statistics in this Press Notice.

4 Charges for credit and deposits or downpayments are excluded from the figures of new credit advanced which thus represent the amount of credit advanced during the period. Figures for retailers are estimated from the value of their self-financed credit sales, which include both charges and deposits. The figures for retailers' credit sales include sales on budget and other running-account agreements and exclude credit sales financed by banks, finance houses, and other specialist credit grantors.

5 Amounts outstanding are the amounts owed, excluding unearned charges, on credit agreements of all types at the end of the period, irrespective of the period in which credit was advanced. Unearned credit charges are those charges, mainly interest, included at the outset of a fixed-sum credit agreement on the assumption that the agreement lasts its full term.

6 Further definitions are given at the foot of the tables accompanying this Press Notice.

7 Full results of the inquiries which collect the monthly information on credit are published by HM Stationery Office in Business Monitor SDM6 - Credit business of finance houses and other specialist credit grantors - and in Business Monitor SDM8 - Credit business of retailers. Both may be obtained on subscription (£17.50 each title per annum) from HM Stationery Office PO Box 569, London SE1 9NH. Individual copies are available, price £3.20 each from:
The Library, Business Statistics Office, Government Buildings, Cardiff Road, Newport GWENT. Telephone: Newport (0633) 222973.

8 Non-press calls to 01-215 6400.

TABLE 1

TOTAL CREDIT BUSINESS OF FINANCE HOUSES, OTHER SPECIALIST CREDIT GRANTORS AND BUILDING SOCIETIES, RETAILERS AND ON BANK CREDIT CARDS (SEASONALLY ADJUSTED)

£ Million

	NEW CREDIT ADVANCED					TOTAL AMOUNT OUTSTANDING (a)	
	TOTAL (c)	FINANCE HOUSES AND OTHER SPECIALIST CREDIT GRANTORS (b): FIXED SUM (d)	FINANCE HOUSES AND OTHER SPECIALIST CREDIT GRANTORS (b): RUNNING ACCOUNT	BANK CREDIT CARDS	RETAILERS (e)	CHANGE	AMOUNT AT END OF PERIOD
1983	10,524	6,840			3,684	2,246	12,199
1984	11,507	7,662			3,845	2,159	14,358
1985	12,996	8,727			4,269	2,586	16,944
1986	31,515	10,720	3,045	12,916	4,834	2,952	23,772
1985 2nd Qtr	3,083	2,030			1,053	533	15,477
3rd Qtr	3,374	2,293			1,081	745	16,222
4th Qtr	3,436	2,336			1,100	722	16,944
1986 1st Qtr	7,375	2,655	648	2,926	1,146	980	21,800
2nd Qtr	7,739	2,640	793	3,115	1,191	418	22,218
3rd Qtr	8,223	2,722	839	3,395	1,267	968	23,186
4th Qtr	8,178	2,703	765	3,480	1,230	586	23,772
1987 1st Qtr	8,881	3,021	745	3,874	1,241	1,012	24,784
1986 MAR	2,372	802	238	954	378	325	21,800
APR	2,717	969	251	1,093	404	120	21,920
MAY	2,409	819	263	942	385	117	22,037
JUN	2,613	852	279	1,080	402	181	22,218
JUL	2,685	885	278	1,107	415	219	22,437
AUG	2,668	890	289	1,068	421	302	22,739
SEP	2,870	947	272	1,220	431	447	23,186
OCT	2,759	925	269	1,152	413	247	23,433
NOV	2,635	843	243	1,129	420	18	23,451
DEC	2,784	935	253	1,199	397	321	23,772
1987 JAN	2,695	870	237	1,177	411	320	24,092
FEB	2,949	1,033	225	1,276	415	323	24,415
MAR	3,237	1,118	283	1,421	415	369	24,784
APR	3,080R	1,066R	309R	1,289	416	483R	25,267R
MAY	3,043	1,077	284	1,268	414	380	25,647
1986 DEC-FEB '87	8,428	3,553		3,652	1,223	964	24,415
1987 MAR-MAY	9,360	4,137		3,978	1,245	1,232	25,647
Percentage increase over previous quarter	11	16		9	2	28	5

—— indicates a break in the series

R = revised

NOTES (a) Until December 1985 excluding amounts outstanding on Bank Credit Cards and block discounted agreements.

(b) Including Building Societies. See Table 2 for an analysis into agreements with consumers and agreements with businesses.

(c) Until December 1985 includes only direct fixed-sum business of Finance Houses and other specialist Credit Grantors and advances by retailers.

(d) From January 1986 including new credit on block discounted agreements.

(e) Self-financed credit advanced by clothing retailers, household goods retailers, mixed retail business (other than Co-operative Societies) and general mail-order houses only.

TABLE 2

TOTAL CREDIT BUSINESS OF FINANCE HOUSES , OTHER SPECIALIST CREDIT GRANTORS AND BUILDING SOCIETIES (SEASONALLY ADJUSTED)

£ Million

	NEW CREDIT ADVANCED				TOTAL AMOUNTS OUTSTANDING		
	AGREEMENTS WITH CONSUMERS (b)		AGREEMENTS WITH BUSINESSES (c)		FIXED SUM AGREEMENTS (a)	RUNNING ACCOUNT AGREEMENTS	DEALER STOCK FUNDING LOANS (d)
	FIXED SUM CREDIT	RUNNING ACCOUNT CREDIT	FIXED SUM CREDIT(a)	RUNNING ACCOUNT CREDIT			
1983	4,470		2,370		9,378	995	652
1984	5,092		2,570		11,183	1,233	789
1985	6,168		2,559		13,165	1,642	939
1986	7,251	3,025	3,469	20	14,778	2,082	1,019
1985 2nd Qtr	1,401		629		12,074	1,403	908
3rd Qtr	1,661		632		12,660	1,503	971
4th Qtr	1,725		611		13,165	1,642	939
1986 1st Qtr	1,833	644	822	4	13,858	1,755	1,027
2nd Qtr	1,781	788	859	5	13,959	1,856	989
3rd Qtr	1,852	835	870	4	14,363	1,957	1,006
4th Qtr	1,785	758	918	7	14,778	2,082	1,019
1987 1st Qtr	2,061	742	960	3	15,370	2,187	964
1986 MAR	539	237	263	1	13,858	1,755	1,027
APR	650	250	319	1	13,892	1,787	987
MAY	558	262	261	1	13,942	1,810	982
JUN	573	276	279	3	13,959	1,856	989
JUL	612	277	273	1	14,032	1,894	1,026
AUG	606	288	284	1	14,190	1,922	989
SEP	634	270	313	2	14,363	1,957	1,006
OCT	607	265	318	4	14,549	2,013	1,080
NOV	570	241	273	2	14,637	2,044	1,024
DEC	608	252	327	1	14,778	2,082	1,019
1987 JAN	593	236	277	1	15,016	2,141	939
FEB	703	224	330	1	15,191	2,165	936
MAR	765	282	353	1	15,370	2,187	964
APR	753R	308R	313	1	15,707R	2,200R	957
MAY	743	283	334	1	16,033	2,215	1,021
1986 DEC-FEB '87	2,616		937		15,191	2,165	936
1987 MAR-MAY	3,134		1,003		16,033	2,215	1,021
Percentage increase over previous quarter	20		7		6	2	9

indicates a break in the series

R = revised

NOTES

(a) From January 1986 including block discounted agreements.

(b) Until December 1985 figures are for consumer credit agreements regulated under the Consumer Credit Act 1974. These comprise non-exempt agreements involving the provision of credit not exceeding £15,000 (£5,000 before 20 May 1985) to individuals.

(c) Until December 1985 figures are for credit agreements not regulated under the Consumer Credit Act 1974, entered into by companies which also enter into regulated credit agreements.

(d) Figures in this column are excluded from amounts oustanding in Table 1.

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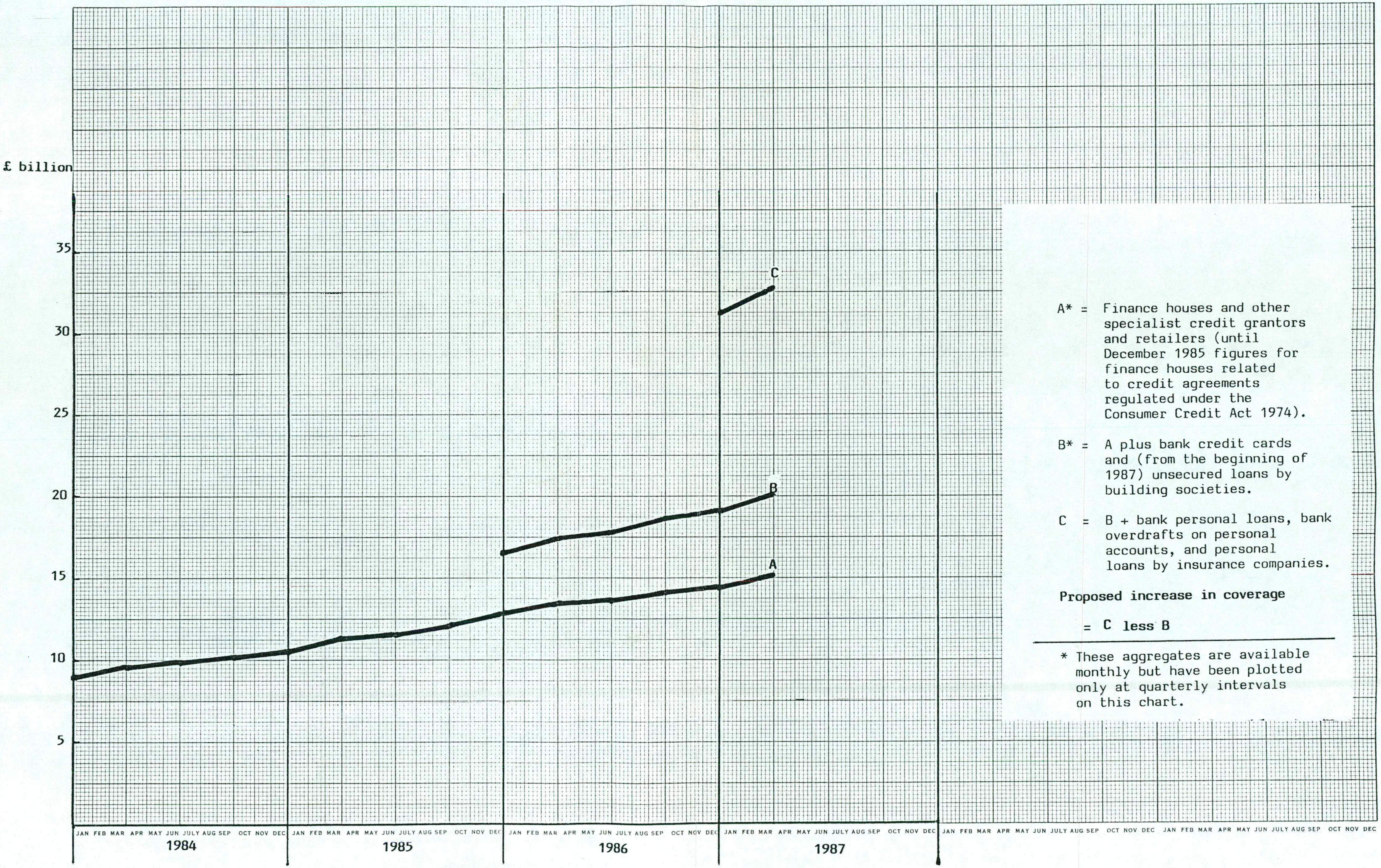
PAST, PRESENT AND PROPOSED FUTURE COVERAGE OF DTI PRESS NOTICE ON CREDIT BUSINESS

Amounts outstanding on agreements with consumers (seasonally adjusted)



Reference RP

To:

SECRETARY OF STATE

(Circulation list attached)

From:

PETER RICHARDSON
S2C
Room 242
Sanctuary Buildings
215 6265

3 July 1987

CREDIT BUSINESS IN MAY

A Press Notice giving details of credit business in May is attached for information. This will be issued at 11.30 am on Monday, 6 July. As usual, the contents should be treated as confidential until then.

P H Richardson.

P H RICHARDSON

CODE 18-78

CONFIDENTIAL UNTIL 11.30 HOURS ON DAY OF RELEASE

DTI Press Notice

Department of Trade and Industry
1 Victoria Street SW1H 0ET
Press Office: 01-215 4471/4475
Out of hours: 01-215 7877

No 87/433

6 July 1987

CREDIT BUSINESS IN MAY

During May £3.0 billion of **new credit** was advanced by finance houses, other specialist credit grantors, retailers and on bank credit cards. This was below the levels of the previous two months, the fall being shown by all types of credit grantor.

Total advances in the latest three months, March to May, were 11 per cent higher than in the previous three months. Lending by finance houses and other specialist credit grantors increased by 16 per cent between the two periods. Within this total, lending to consumers increased by 20 per cent and lending to businesses increased by 7 per cent. Advances on bank credit cards increased by 9 per cent between the two periods. Retailers advanced 2 per cent more in the latest three months than in the previous three months.

There was an increase of £0.4 billion in **amounts outstanding** to finance houses, other specialist credit grantors, retailers and on bank credit cards between end-April and end-May. The total amount outstanding at end-May was £25.6 billion, 5 per cent more than the total three months earlier.

Notes to Editors

1 All figures are quoted after seasonal adjustment.

2 Table 1 covers the credit business of finance houses, other specialist credit grantors and building societies, retailers and on bank credit cards. Table 2 covers the business of finance houses, other specialist credit grantors and building societies only, but provides an analysis of new credit advanced to consumers and businesses. The credit advances shown in Table 1 for retailers and bank credit cards are mainly to consumers. A high proportion of credit advances in certain types of agreement, notably on bank credit cards and by mail order houses, is repaid within a month, reflecting the use of such agreements as a method of payment rather than as a means of obtaining credit.

3 From January 1986 the statistics include new credit advances by finance houses and other specialist credit grantors on running account agreements on which information was not collected previously. Lending on bank credit cards is also included for the first time in the January 1986 statistics. Unsecured loans by building societies, which are advanced under the provisions of the Building Societies Act 1986, are included from January 1987. Lending by banks, other than on bank credit cards, and by companies where the group specialises in lending to other companies only are excluded from the statistics in this Press Notice.

4 Charges for credit and deposits or downpayments are excluded from the figures of new credit advanced which thus represent the amount of credit advanced during the period. Figures for retailers are estimated from the value of their self-financed credit sales, which include both charges and deposits. The figures for retailers' credit sales include sales on budget and other running-account agreements and exclude credit sales financed by banks, finance houses, and other specialist credit grantors.

5 Amounts outstanding are the amounts owed, excluding unearned charges, on credit agreements of all types at the end of the period, irrespective of the period in which credit was advanced. Unearned credit charges are those charges, mainly interest, included at the outset of a fixed-sum credit agreement on the assumption that the agreement lasts its full term.

6 Further definitions are given at the foot of the tables accompanying this Press Notice.

7 Full results of the inquiries which collect the monthly information on credit are published by HM Stationery Office in Business Monitor SDM6 - Credit business of finance houses and other specialist credit grantors - and in Business Monitor SDM8 - Credit business of retailers. Both may be obtained on subscription (£17.50 each title per annum) from HM Stationery Office PO Box 569, London SE1 9NH. Individual copies are available, price £3.20 each from:
The Library, Business Statistics Office, Government Buildings, Cardiff Road, Newport GWENT. Telephone: Newport (0633) 222973.

8 Non-press calls to 01-215 6400.

TABLE 1

TOTAL CREDIT BUSINESS OF FINANCE HOUSES, OTHER SPECIALIST CREDIT GRANTORS AND BUILDING SOCIETIES, RETAILERS AND ON BANK CREDIT CARDS (SEASONALLY ADJUSTED)

£ Million

	NEW CREDIT ADVANCED					TOTAL AMOUNT OUTSTANDING (a)	
	TOTAL	FINANCE HOUSES AND OTHER SPECIALIST CREDIT GRANTORS (b)		BANK CREDIT CARDS	RETAILERS	CHANGE	AMOUNT AT END OF PERIOD
	(c)	FIXED SUM (d)	RUNNING ACCOUNT		(e)		
1983	10,524	6,840			3,684	2,246	12,199
1984	11,507	7,662			3,845	2,159	14,358
1985	12,996	8,727			4,269	2,586	16,944
1986	31,515	10,720	3,045	12,916	4,834	2,952	23,772
1985 2nd Qtr	3,083	2,030			1,053	533	15,477
3rd Qtr	3,374	2,293			1,081	745	16,222
4th Qtr	3,436	2,336			1,100	722	16,944
1986 1st Qtr	7,375	2,655	648	2,926	1,146	980	21,800
2nd Qtr	7,739	2,640	793	3,115	1,191	418	22,218
3rd Qtr	8,223	2,722	839	3,395	1,267	968	23,186
4th Qtr	8,178	2,703	765	3,480	1,230	586	23,772
1987 1st Qtr	8,881	3,021	745	3,874	1,241	1,012	24,784
1986 MAR	2,372	802	238	954	378	325	21,800
APR	2,717	969	251	1,093	404	120	21,920
MAY	2,409	819	263	942	385	117	22,037
JUN	2,613	852	279	1,080	402	181	22,218
JUL	2,685	885	278	1,107	415	219	22,437
AUG	2,668	890	289	1,068	421	302	22,739
SEP	2,870	947	272	1,220	431	447	23,186
OCT	2,759	925	269	1,152	413	247	23,433
NOV	2,635	843	243	1,129	420	18	23,451
DEC	2,784	935	253	1,199	397	321	23,772
1987 JAN	2,695	870	237	1,177	411	320	24,092
FEB	2,949	1,033	225	1,276	415	323	24,415
MAR	3,237	1,118	283	1,421	415	369	24,784
APR	3,080R	1,066R	309R	1,289	416	483R	25,267R
MAY	3,043	1,077	284	1,268	414	380	25,647
1986 DEC-FEB '87	8,428	3,553		3,652	1,223	964	24,415
1987 MAR-MAY	9,360	4,137		3,978	1,245	1,232	25,647
Percentage increase over previous quarter	11	16		9	2	28	5

——— indicates a break in the series

R = revised

NOTES (a) Until December 1985 excluding amounts outstanding on Bank Credit Cards and block discounted agreements.

(b) Including Building Societies. See Table 2 for an analysis into agreements with consumers and agreements with businesses.

(c) Until December 1985 includes only direct fixed-sum business of Finance Houses and other specialist Credit Grantors and advances by retailers.

(d) From January 1986 including new credit on block discounted agreements.

(e) Self-financed credit advanced by clothing retailers, household goods retailers, mixed retail businesses (other than Co-operative Societies) and general mail-order houses only.

TABLE 2

TOTAL CREDIT BUSINESS OF FINANCE HOUSES , OTHER SPECIALIST CREDIT GRANTORS AND BUILDING SOCIETIES (SEASONALLY ADJUSTED)

£ Million

	NEW CREDIT ADVANCED				TOTAL AMOUNTS OUTSTANDING		
	AGREEMENTS WITH CONSUMERS (b)		AGREEMENTS WITH BUSINESSES (c)		FIXED SUM AGREEMENTS (a)	RUNNING ACCOUNT AGREEMENTS	DEALER STOCK FUNDING LOANS (d)
	FIXED SUM CREDIT	RUNNING ACCOUNT CREDIT	FIXED SUM CREDIT(a)	RUNNING ACCOUNT CREDIT			
1983	4,470	.	2,370		9,378	995	652
1984	5,092		2,570		11,183	1,233	789
1985	6,168		2,559		13,165	1,642	939
1986	7,251	3,025	3,469	20	14,778	2,082	1,019
1985 2nd Qtr	1,401		629		12,074	1,403	908
3rd Qtr	1,661		632		12,660	1,503	971
4th Qtr	1,725		611		13,165	1,642	939
1986 1st Qtr	1,833	644	822	4	13,858	1,755	1,027
2nd Qtr	1,781	788	859	5	13,959	1,856	989
3rd Qtr	1,852	835	870	4	14,363	1,957	1,006
4th Qtr	1,785	758	918	7	14,778	2,082	1,019
1987 1st Qtr	2,061	742	960	3	15,370	2,187	964
1986 MAR	539	237	263	1	13,858	1,755	1,027
APR	650	250	319	1	13,892	1,787	987
MAY	558	262	261	1	13,942	1,810	982
JUN	573	276	279	3	13,959	1,856	989
JUL	612	277	273	1	14,032	1,894	1,026
AUG	606	288	284	1	14,190	1,922	989
SEP	634	270	313	2	14,363	1,957	1,006
OCT	607	265	318	4	14,549	2,013	1,080
NOV	570	241	273	2	14,637	2,044	1,024
DEC	608	252	327	1	14,778	2,082	1,019
1987 JAN	593	236	277	1	15,016	2,141	939
FEB	703	224	330	1	15,191	2,165	936
MAR	765	282	353	1	15,370	2,187	964
APR	753R	308R	313	1	15,707R	2,200R	957
MAY	743	283	334	1	16,033	2,215	1,021
1986 DEC-FEB '87	2,616		937		15,191	2,165	936
1987 MAR-MAY	3,134		1,003		16,033	2,215	1,021
Percentage increase over previous quarter	20		7		6	2	9

—— indicates a break in the series R = revised

NOTES

(a) From January 1986 including block discounted agreements.

(b) Until December 1985 figures are for consumer credit agreements regulated under the Consumer Credit Act 1974. These comprise non-exempt agreements involving the provision of credit not exceeding £15,000 (£5,000 before 20 May 1985) to individuals.

(c) Until December 1985 figures are for credit agreements not regulated under the Consumer Credit Act 1974, entered into by companies which also enter into regulated credit agreements.

(d) Figures in this column are excluded from amounts oustanding in Table 1.

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Prime Minister's Office

Chancellor's Office

Sir Terence Burns	-	Treasury
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Mr J Alexander	-	"

4562/008

CONFIDENTIAL
UNTIL 11.30am 10 AUGUST

FROM: P H BROOK
DATE: 7 August 1987

PHP

1. MR ~~PERETZ~~

2. ECONOMIC SECRETARY

cc Chancellor — Paymaster-General
Sir P Middleton
Sir T Burns
Sir G Littler
Mr Cassell
Mr Sedgwick
Mr Culpin
Mr C W Kelly
Miss Noble
Mr Pike
Mr Richardson o/r
Mr P S Hall

This is the new style DTI press release to which we have agreed — and which from now on will once a quarter include the figures in table 2 col 4 for bank personal loans. We've included some briefing for DTI, below, though as it happens there's nothing at all exciting in the figures this time. For the future I suggest we might circulate a much shorter note with the figures when they arrive. But we would of course draw any points of interest to your attention: and provide DTI with briefing if necessary.

DLP 7/8

DTI PRESS NOTICE ON CONSUMER CREDIT

(All figures seasonally adjusted unless specified otherwise.)

The DTI press notice on credit business statistics in June will be published at 11.30 am on Monday 10 August.

Summary

2. The statistics show that the total amount outstanding of consumer credit was £33.8 billion at the end of the second quarter of 1987, an increase of about £1.5 billion (4.7 per cent) on the first quarter. This compares with an increase in bank lending to the non-bank private sector over the same period of about £8.6 billion (4.9 per cent). Of this about £1.4 billion (unadjusted) has already been identified in the London and Scottish Banks' press releases as being for 'consumption'. Seasonally adjusted this figure would be slightly lower.

3. The annual growth rate of outstanding consumer credit rose from 9.5 per cent to the end of the first quarter of 1987 to 13.4 per cent to the end of the second quarter.

4. Within total consumer credit outstanding, borrowing via bank credit cards (Access and Visa) stood at £5.2 billion at the end of the second quarter, an increase of £260 million (5.3 per cent) during the quarter.

CONFIDENTIAL

UNTIL 11 30 am 10 AUGUST

5. Figures for total personal sector debt (which includes loans for house purchase) are only available for the first quarter of 1987. They show that total consumer credit was 15.2 per cent, and borrowing via bank credit cards (Access and Visa) was 2.3 per cent, of personal sector debt. Both figures are unchanged from the final quarter of 1986.

Press Briefing

6. Detailed questions on the statistics are clearly for DTI's press office to answer. We suggest that Treasury press office only comment if asked about monetary policy aspects. In these circumstances, we propose the press office takes the line that there is very little new in these statistics, most of which was known from the money and CLSB figures which have been published already. I attach a background note and a very short brief making this point. It also includes a defensive point for use if asked about a link between consumer credit and the rise in interest rates. This is drawn from the points made by the Chancellor on BBC 1 News Afternoon on Thursday 6 August. A copy of the relevant part of the transcript is also attached.

7. The final attachment is a copy of the DTI press release.

8. I would be grateful for any comments on the press briefing early on Monday 10 August.

P. Brook

P H BROOK

DTI CONSUMER CREDIT STATISTICS

Background Note

From August 10 the coverage and presentation of the monthly DTI press notice on credit business statistics is to change. The main change in coverage is that henceforth the press notice will include quarterly data on personal loans, and overdrafts on personal accounts, not exceeding £15,000 (the upper limit of personal loans to individuals regulated under the Consumer Credit Act). The figures which will appear in the August press release will be a sub-set of the bank lending figures already published in the June provisional money figures on 20 July and in the final money figures for June on 29 July. CLSB lending to the personal sector in June has also already been separately identified in the CLSB press release of 20 July. A further minor addition to the coverage is that loans by insurance companies to individuals will be included.

2. Previously the main emphasis of the press notice has been new credit advances (ie. gross lending, excluding repayments). This included 'turnover' on bank credit cards and their importance in consumer credit has thus been exaggerated to the extent that these are used as a method of payment rather than as a means of obtaining credit. The revised presentation will give prominence to changes in amount of credit outstanding.

Press Briefing

Detailed questions to be referred to DTI press office.

IF ASKED about monetary policy aspects IDT could draw on the following points:

- very little that is new in DTI statistics. Money and CLSB figures already published to end of June. Consumer credit represents only about 15 per cent of total personal debt [and less than 5 per cent of personal debt takes form of credit card lending].

- Interest rates raised in reaction to consumer credit boom? No. Chancellor made clear that looking at economic and financial indicators as a whole it was right to tighten monetary conditions a little. (See attached)

CHANCELLOR - INTERVIEW ON INTEREST RATE RISE

Transcript from: BBC 1 tv, News Afternoon, 6 August 1987

INTERVIEWER: ... And now back to today's main story, the news that interest rates are going up by 1%. Joining me now live from Downing St is the Chancellor of the Exchequer Nigel Lawson. Mr Lawson what's the reason behind this increase, is it too much consumer debt?

CHANCELLOR: No, it's looking at the economic and financial indicators as a whole and deciding that to maintain the sound monetary conditions which have brought inflation down and kept it down it's necessary to have a slight tightening of monetary conditions which means putting interest rates up by 1%.

INTERVIEWER: We've heard a lot of talk about consumer debt, too much using our credit cards and so on, so that wasn't a factor?

CHANCELLOR: No, credit cards are a very minor matter in total consumer debt. But quite apart from that it was a matter of looking at all the indicators together and judging, as I have done throughout the time that I've been Chancellor from time to time, judging that it was necessary to put interest rates up a little bit in order to maintain the sound financial conditions which have made this country the fastest growing economy of all the major countries in the world and kept inflation low. And that's what I intend to stick to.

DTI Press Notice

CONFIDENTIAL UNTIL 11.30 HOURS ON DAY OF RELEASE

Department of Trade and Industry
1 Victoria Street SW1H 0ET
Press Office: 01-215 4471/4475
Out of hours: 01-215 7877

Number 87/465

7 August 1987

CREDIT BUSINESS IN JUNE

During June the **change in amounts outstanding on consumer credit agreements** with finance houses, other specialist credit grantors, building societies, retailers and on bank credit cards was £0.4 billion (see **Table 1**). This compared to an increase in May of £0.3 billion.

The increase in the latest three months, April to June, was £1.1 billion, slightly more than the corresponding figure of £1.0 billion in the previous three months. Within the total, the increase shown by finance houses, other specialist credit grantors and building societies was £0.8 billion in the most recent period compared to £0.6 billion in the previous one. The increases for bank credit cards and retailers in the latest three months were much the same as in the previous period. In the period April to June they were £0.3 billion for bank credit cards and £0.1 billion for retailers.

Bank loans on personal accounts showed an increase in amounts outstanding of £0.5 billion, higher than the previous quarter's value of £0.2 billion (see **Table 2**). Including these loans and loans by insurance companies, figures for which are available only quarterly, gives a **total increase in consumer credit** in the April to June quarter of £1.5 billion, up from £1.2 billion in the preceding quarter. At the end of the quarter, the **total amount outstanding on consumer credit agreements** was £33.8 billion, 5 per cent more than the total at the end of the previous quarter.

MORE/...

New credit advanced to consumers in June by finance houses, other specialist credit grantors, building societies, retailers and on bank credit cards amounted to £3.0 billion, compared to a total of £2.7 billion in May (see **Table 2**). The total for the three months April to June was 7 per cent higher than that for the previous three months.

In June there was a **change in amounts outstanding on agreements with businesses** by finance houses, other specialist credit grantors and building societies of £0.2 billion (see **Table 1**). The total change in the latest three months was £0.4 billion compared to no change in the preceding three months. At the end of June the total value of the outstanding amounts was £6.1 billion.

Changes to Credit Business Press Notice

1 Starting from this month there are changes in the coverage and presentation of the statistics.

2 The coverage of the data has been expanded to include loans by banks (monetary sector institutions other than those included in finance houses and other specialist credit grantors) on personal accounts, where the amount outstanding does not exceed £15,000, and loans by insurance companies to individuals. Figures for such loans which are available only quarterly, are now included in the quarterly totals in Table 2 to give statistics on total consumer credit. The main sources of finance for house purchase are, by definition, excluded.

3 All institutions lending to individuals for consumption are covered by these quarterly totals, although, in the case of banks, only personal loans where the amount outstanding does not exceed £15,000 are included. Loans to businesses by retailers and on bank credit cards are included in total consumer credit as they cannot be separately identified. They are thought to be small in relation to loans to consumers.

4 There are also changes to the presentation of the data. The text now concentrates on changes in amounts outstanding. Previously the main emphasis was on new credit advanced. This overstated the level of credit advances when, for example, bank credit cards were used as the method of payment rather than as a means of obtaining credit. Changes in amounts outstanding are a better indicator as repayments by consumers are taken into account.

5 In Tables 1, 2 and 3 separate totals are given for agreements with consumers and all agreements. The latter includes lending to businesses. Such lending is only part of total lending to businesses. Lending by banks and by finance houses and other specialist credit grantors, where the group specialises in lending to other companies only are not included in the statistics.

NOTES TO EDITORS

1 All figures are quoted after seasonal adjustment. The seasonal adjustments of bank loans on personal account and of credit card lending are subject to greater uncertainty than the seasonal adjustments of the other data owing to the shortness of the series.

2 **Table 1** covers amounts outstanding and changes in amounts outstanding to finance houses, other specialist credit grantors and building societies, retailers and on bank credit cards. Loans by retailers and on bank credit cards are mainly to consumers and are treated as consumer agreements. Loans by finance houses, other specialist credit grantors and building societies, are split into agreements with consumers and agreements with businesses and the two components are shown separately.

3 **Table 2** includes the same data as Table 1 with the addition of loans by banks (monetary sector institutions other than those included in finance houses and other specialist credit grantors) on personal accounts, where the amount outstanding does not exceed £15,000, and by insurance companies to individuals, excluding loans for house purchase and bridging finance. These figures are available only quarterly. This table therefore contains a quarterly series which covers all institutions which provide finance for consumers.

4 **Table 3** shows new credit advanced by finance houses, other specialist credit grantors and building societies, retailers and on bank credit cards. The coverage is the same as for Table 1 except that dealer stock funding loans by finance houses to businesses are excluded.

5 Unsecured loans by building societies, which are advanced under the terms of the Building Societies Act 1986, are included from January 1987. Amount outstanding on bank loans on personal accounts are available from end December 1986 only. Lending by finance houses and other specialist credit grantors where the group specialises in lending to other companies only are excluded from the statistics in this Press Notice.

6 Further definitions are given at the foot of the tables accompanying this Press Notice.

7 Full results of the inquiries which collect the monthly information on credit are published by H M Stationery Office in Business Monitor SDM6 - Credit business of finance houses and other specialist credit grantors - and in Business Monitor SDM8 - Credit business of retailers. Both may be obtained on subscription (£17.50 each title per annum) from H M Stationery Office P O Box 569, London SE1 9NH. Individual copies are available, price £3.20 each from:

The Library,
Business Statistics Office,
Government Buildings,
Cardiff Road,
Newport, GWENT.
Telephone: Newport (0633) 222973.

8 Non-press calls to 01-215 3138

TABLE 1

CHANGES IN AMOUNTS OUTSTANDING TO FINANCE HOUSES, OTHER SPECIALIST CREDIT GRANTORS AND BUILDING SOCIETIES, RETAILERS AND ON BANK CREDIT CARDS. (SEASONALLY ADJUSTED)

£ Million

	AGREEMENTS WITH CONSUMERS				AGREEMENTS WITH BUSINESSES	TOTAL AGREEMENTS
	TOTAL	RETAILERS (a)	BANK CREDIT CARDS	FINANCE HOUSES, OTHER SPECIALIST CREDIT GRANTORS AND BUILDING SOCIETIES ON AGREEMENTS WITH CONSUMERS	BUSINESSES	
AMOUNTS OUTSTANDING AT END OF PERIOD						
1986	19,063	2,231	4,681	12,151	5,728	24,791
1987 JUN	21,082	2,354	5,189	13,539	6,106	27,188
CHANGES IN AMOUNTS OUTSTANDING						
1986	2,437	94	891	1,452	596	3,033
1986 1st Qtr	855	39	221	595	214	1,069
2nd Qtr	346	3	213	130	34	380
3rd Qtr	792	107	356	329	193	985
4th Qtr	444	-55	101	398	155	599
1987 1st Qtr	952	67	248	637	5	957
2nd Qtr	1,067	56	260	751	373	1,440
1986 JUN	167	9	109	49	21	188
JUL	183	28	80	75	73	256
AUG	217	34	82	101	48	265
SEP	392	45	194	153	72	464
OCT	194	-81	86	189	127	321
NOV	-15	12	-113	86	-23	-38
DEC	265	14	128	123	51	316
1987 JAN	257	8	15	234	-17	240
FEB	296	27	97	172	24	320
MAR	399	32	136	231	-2	397
APR	410	20	113	277	66	476
MAY	294R	20	19	255R	141	435R
JUN	363	16	128	219	166	529
1987 JAN-MAR	952	67	248	637	5	957
1987 APR-JUN	1,067	56	260	751	373	1,440

R = revised

NOTES

(a) Self financed credit advanced by clothing retailers, household goods retailers mixed retail businesses (other than Co-operative societies) and general mail-order houses only.

(b) Data were not collected on a consistent basis for all types of credit grantor prior to 1986. The following table gives figures for changes in amounts outstanding which are available:

£ Million

	1983	1984	1985
Retailers	132	116	195
Finance Houses etc.	2,286	2,180	2,541

TABLE 2

CHANGES IN AMOUNTS OUTSTANDING TO FINANCE HOUSES, OTHER SPECIALIST CREDIT GRANTORS AND BUILDING SOCIETIES, RETAILERS, BANKS ON CREDIT CARDS AND PERSONAL ACCOUNTS AND TO INSURANCE COMPANIES ON CONSUMER LOANS.

(SEASONALLY ADJUSTED)

£ Million

	AGREEMENTS WITH CONSUMERS						AGREEMENTS WITH BUSINESSES	TOTAL AGREEMENTS (a)
	TOTAL (a)	RETAILERS (b)	BANKS (c)		INSURANCE COMPANIES	FINANCE HOUSES, OTHER SPECIALIST CREDIT GRANTORS AND BUILDING SOCIETIES ON AGREEMENTS WITH		
			CREDIT CARDS	LOANS ON PERSONAL ACCOUNTS (d)		CONSUMERS	BUSINESSES	
AMOUNT OUTSTANDING AT END OF PERIOD								
1986	31,095	2,231	4,681	11,228	804	12,151	5,728	36,823
1987 1st Qtr	32,267	2,298	4,929	11,440	812	12,788	5,733	38,000
2nd Qtr	33,799	2,354	5,189	11,895	822E	13,539	6,106	39,905
CHANGES IN AMOUNTS OUTSTANDING								
1986	2,496	94	891		59	1,452	596	3,092
1986 1st Qtr	858	39	221		3	595	214	1,072
2nd Qtr	360	3	213		14	130	34	394
3rd Qtr	806	107	356		14	329	193	999
4th Qtr	472	-55	101		28	398	155	627
1987 1st Qtr	1,172	67	248	212	8	637	5	1,177
2nd Qtr	1,532	56	260	455	10E	751	373	1,905

—— indicates a break in the series

R = revised
E = estimated

NOTES

(a) Changes in amounts outstanding in 1986 exclude bank loans on personal accounts.

(b) Self-financed advances by clothing retailers, household goods retailers mixed retail businesses (other than Co-operative societies) and general mail order houses only.

(c) Monetary sector institutions other than those included in finance houses and other specialist credit grantors.

(d) Amounts outstanding on bank loans on personal accounts, not exceeding £15,000, excluding bridging loans and house purchase finance.

TABLE 3

NEW CREDIT ADVANCED BY FINANCE HOUSES, OTHER SPECIALIST CREDIT GRANTORS AND BUILDING SOCIETIES, RETAILERS AND ON BANK CREDIT CARDS. (SEASONALLY ADJUSTED)

£ Million

	AGREEMENTS WITH CONSUMERS				AGREEMENTS WITH BUSINESSES	TOTAL AGREEMENTS
	TOTAL	RETAILERS (a)	BANK CREDIT CARDS	FINANCE HOUSES, OTHER SPECIALIST CREDIT GRANTORS AND BUILDING SOCIETIES ON AGREEMENTS WITH CONSUMERS	BUSINESSES (b)	
1986	28,026	4,834	12,916	10,276	3,489	31,515
1986 1st Qtr	6,549	1,146	2,926	2,477	826	7,375
2nd Qtr	6,875	1,191	3,115	2,569	864	7,739
3rd Qtr	7,349	1,267	3,395	2,687	874	8,223
4th Qtr	7,253	1,230	3,480	2,543	925	8,178
1987 1st Qtr	7,918	1,241	3,874	2,803	963	8,881
2nd Qtr	8,445	1,272	3,997	3,176	1,029	9,474
1986 JUN	2,331	402	1,080	849	282	2,613
JUL	2,411	415	1,107	889	274	2,685
AUG	2,383	421	1,068	894	285	2,668
SEP	2,555	431	1,220	904	315	2,870
OCT	2,437	413	1,152	872	322	2,759
NOV	2,360	420	1,129	811	275	2,635
DEC	2,456	397	1,199	860	328	2,784
1987 JAN	2,417	411	1,177	829	278	2,695
FEB	2,618	415	1,276	927	331	2,949
MAR	2,883	415	1,421	1,047	354	3,237
APR	2,766	416	1,289	1,061	314	3,080
MAY	2,697R	414	1,268	1,015R	335	3,032R
JUN	2,982	442	1,440	1,100	380	3,362
1987 JAN-MAR	7,918	1,241	3,874	2,803	963	8,881
1987 APR-JUN	8,445	1,272	3,997	3,176	1,029	9,474
Percentage increase over previous quarter	7	2	3	13	7	7

R = revised

NOTES

(a) Self financed credit advanced by clothing retailers, household goods retailers, mixed retail businesses (other than Co-operative societies) and general mail-order houses only.

(b) Excluding dealer stock funding. These agreements are included in tables 1 and 2.

3456/002

CONFIDENTIAL

FROM: R FELLGETT
DATE: 7 August 1987

1. MR HAWTIN
2. CHANCELLOR

cc PS/Chief Secretary
PS/Paymaster General
Sir P Middleton
Mr F E R Butler
Mr Anson
Mr Gilmore
Mr Potter (o/r)
Miss Sinclair
Mr Tyrie
PS/TR
Mr Houghton (IR)
Mr Heard (IR)
Mr Battersby (IR)

Ch, Content to write as proposed? AF 10/8

OK. on Shaw

EFFECTS OF DOMESTIC REVALUATION

You asked (Mr Allan's minute of 4 August - received yesterday) for advice on Mr Ridley's letter of 31 July.

2. Mr Houghton's minute of 31 July to the Chief Secretary contained some background, and sought Treasury Ministers' views about going ahead with the study proposed by DOE.

3. Central Treasury was unaware of any remit to mount a further study until we saw Mr Houghton's minute of 31 July. We have since discovered from DOE that, in their view, the remit was contained in a letter from No 10 to DOE of 2 July, from which we have seen only the attached paragraph. This talks about marshalling all the facts, and makes reference to past revaluations and the Scottish experience, but does not explicitly commission a new sample study of capital and rental values of domestic property. So far as we are aware, the idea of a new study arose within DOE.

Because it is all No 10 are prepared to release

CONFIDENTIAL

4. I understand from the Revenue that their first involvement was an approach in mid-July by DOE officials to Valuation Office officials about the possibility of carrying out some urgent work. Such requests are not unprecedented in the normal working relationship on rating matters between DOE and the Valuation Office. Revenue officials made it clear that there were no spare resources available, and that they could not commit themselves to an exercise of such sensitivity without the approval of Treasury Ministers, but it was premature to seek that before DOE Ministers (rather than officials) had indicated their wish to go ahead. As soon as DOE Ministers so indicated, a report was made in Mr Houghton's minute of 31 July.

5. You thought that if this exercise is to be done at all, it must be very rough and ready, using minimal Inland Revenue resources. Any Revenue exercise would use limited resources and they would show Treasury Ministers the results before they were given to DOE.

6. However, it is clear that the DOE are looking for a study with some weight, which they could describe in public as an objective study by VO experts. Anything too rough and ready might not stand up.

7. In any case, it is not clear that a study would produce the answers that the Prime Minister is looking for. It is reasonable to guess that a revaluation (either on rental or capital values) would hit the South and help the North, because house prices have risen faster in London and the South East than elsewhere, and the limited private rented market ought to reflect capital values. But it does not follow that a revaluation would be more unpopular than the community charge, in the sense that there would be more big losers on some definition. A priori, all one can say is that a change from a property to a personal tax is likely to involve more losers than winners, whereas a redistribution of the rates burden would be likely to produce roughly equal numbers of both.

9. As to Inland Revenue resources, Mr Houghton has commented in his minute. All we would wish to add from Central Treasury

is that the Revenue statisticians are working on much more important issues for you, so the study (if it should go ahead) must use the promised DOE statistician.

Conclusion

10. Despite the wording of Mr Ridley's letter, there does not appear to be a clear remit to undertake a further sample study of up-to-date capital or rental values. If there were such a remit, the basic work would fall to the VO. But a rough and ready study might not meet DOE's needs, and might produce results that were unwelcome. In these circumstances, you may wish to query with Mr Ridley whether such a study should go ahead. A draft letter along these lines is attached.

11. FP agree. This advice has also been agreed with the Revenue.

Robin Fellgett

R FELLGETT

3456/003

~~DRAFT~~ LETTER FOR THE CHANCELLOR'S SIGNATURE TO THE SECRETARY OF STATE FOR THE ENVIRONMENT

EFFECTS OF DOMESTIC REVALUATION

Thank you for your letter of 31 July.

I had not earlier heard of a remit from the Prime Minister for an exercise which would involve a sample study by my officials in the Inland Revenue along the lines that you propose. My officials have just seen an extract from a letter dated 2 July from No 10 to your office, but this simply talks about a need to marshal all the facts, and refers in particular to past revaluations and the Scottish example. There is no reference to a new study.

3. A new study would inevitably affect normal work in the Valuation Office. Its existence could leak before the results are available. And we cannot of course guarantee that the conclusions would provide helpful ammunition in our campaign to get the case for a reform of local authority finance across more effectively, as the Prime Minister requested.

4. In these circumstances, I would prefer not to mount a new sample study but rather to rely on historical evidence of the evident unpopularity of revaluations, as was originally suggested.

[N.L]

EXTRACT FROM DRN TO DOE 2.7.87
LOCAL AUTHORITY FINANCE

The Prime Minister stressed the need for the Government to put across the case for the reform of local authority finance more effectively. A true comparison was not between the existing system and the community charge, but between the system with a revaluation and the community charge. The example set by Scotland, and the controversies surrounding revaluations in the 1960s and early 1970s ought to be pointed out to those who were arguing against the new system. There was a need to marshal all the facts. It would be important in particular to prevent Conservative MPs from committing themselves during the Recess to opposing the reforms.

P.S./CHANCELLOR OF EXCHEQUER, UNCLASSIFIED
H.M.TREASURY.

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SIC EYG
PRESS SUMMARY FOR 26 AUGUST

1. MAIN HEADLINES
STRIKES. COLLECTIVE WAGE BARGAINING.

2. LABOUR
THE GENDAKAMERIE NACIONAL HAS TAKEN OVER YPF INSTALLATIONS AROUND THE COUNTRY AND SENIOR STAFF ARE OPERATING THE PLAZA HUINCAL GAS PLANT IN NEUQUEN. GAS AND PETROL SUPPLIES ARE EFFECTIVELY BACK TO NORMAL AND REFINERY WORKERS ARE EXPECTED TO RESUME WORK SHORTLY. (CLARIN P2)

RAILWAY, TELEPHONE AND DOCK WORKERS WERE ALL ON STRIKC ON 25 AUGUST WITH PARTIAL STRIKES BEING HELD BY TEACHERS AND JUDICIAL EMPLOYEES. STATE BANK WORKERS ARE TO HOLD A PARTIAL STRIKE ON 27 AUGUST AND AEROLINEAS PILOTS MAY TAKE SIMILAR ACTION BEFORE THE END OF THE WEEK. (CLARIN P3-6)

A MINISTRY OF LABOUR ADVISER HAS ANNOUNCED THAT COLLECTIVE BARGAINING INCLUDING WAGES IS TO BEGIN ON 1 SEPTEMBER AND THAT THE RELEVANT DECREE WILL BE ISSUED ON 27 AUGUST. THE UIA HAS SAID IT WILL NOT TAKE PART IN THE TRILATERAL COMMISSION ON COLLECTIVE BARGAINING IF PRICES AND WAGES ARE INCLUDED. (PRENSA 1/6, CRONISTA COMERCIAL P1/3/4)

3. CONSTITUTIONAL REFORM
THE COUNCIL FOR THE CONSOLIDATION OF DEMOCRACY HAS SUBMITTED A REPORT RECOMMENDING ESTABLISHMENT IN ARGENTINA OF A SEMI-PARLIAMENTARY SYSTEM WITH THE POST OF PRIME MINISTER AND THE REELECTION OF THE PRESIDENT. (NACION P16)

4. POLITICAL
PERONIST GUBERNATORIAL CANDIDATE FOR BUENOS AIRES PROVINCE ANTONIO CAFIERO HAS ACCUSED THE GOVERNMENT OF DELIBERATELY PROVOKING LABOUR UNREST TO DISCREDIT PERONISTS BEFORE THE ELECTION. (CLARIN P10)

VICE-PRESIDENT VICTOR MARTINEZ HAS DENIED THE RADICALS ARE PLANNING TO LAUNCH A TERROR CAMPAIGN. (CLARIN P11)

UCEDE GUBERNATORIAL CANDIDATE FOR BUENOS AIRES PROVINCE FREDERICO CLERICI HAS SAID THE RADICAL PARTY ATTEMPTED 3 TIMES TO PURSUADE HIM TO WITHDRAW HIS CANDIDATURE. (NACION P7)

COLUMNIST DANIEL LUPA CLAIMS THE RADICALS STAND TO LOSE AS MANY AS 16 OR 17 NATIONAL DEPUTIES AND HENCE THEIR MAJORITY IN THE LOWER HOUSE OF CONGRESS. THE RADICALS HAVE CONCLUDED THAT THEIR CHANCES OF VICTORY UNDER THE D'HONT SYSTEM ARE BETTER THE MORE SMALL PARTIES THERE ARE COMPETING. THEY HAVE HENCE PROMOTED THE ELECTORAL CAMPAIGN OF SMALL PARTIES IN FEDERAL CAPITAL AND BUENOS AIRES PROVINCE. (PRENSA P1/4)

THE LOSS BY THE RADICALS OF BUENOS AIRES PROVINCE WOULD PROVOKE A MAJOR STRUGGLE WITHIN THE PARTY. (AMBITO P12)

5. MILITARY

DEFENCE MINISTER HORACIO JAUNARENA, VISITING MAR DEL PLATA TO WITNESS A FIRING EXERCISE BY THE 601 AIR DEFENCE GROUP, SAID THERE WAS NO POSSIBILITY OF A COUP D'ETAT& THE GOVERNMENT WAS WORKING FOR AN ADEQUATE NATIONAL DEFENCE LAW AND THE EXISTING BILL, ALREADY APPROVED BY THE SENATE, WOULD NOT BE WITHDRAWN FROM CONGRESS. THE FIRING EXERCISES IN MAR DEL PLATA INCLUDED 2 ROLAND II MISSILES, BOTH OF WHICH REPORTEDLY HIT THEIR TARGETS. (PRENSA P4)

6. ECONOMIC AND FINANCIAL

ON 25 AUGUST THE GOVERNMENT SOLD 291 MILLION AUSTRALES WORTH OF TACAM BONDS WHICH ARE LINKED TO THE OFFICIAL DOLLAR EXCHANGE RATE. (AMBITO P1)

THE CENTRAL BANK YESTERDAY DEVALUED THE AUSTRAL BY 1.62 PER CENT AGAINST THE DOLLAR. FREE MARKET INTEREST RATES ROSE TO 15.5 PER CENT PER MONTH AND THE PARALLEL DOLLAR CLOSED AT 3.05 AUSTRALES. (CLARIN P21)

THE FOREIGN TRADE AND INDUSTRY IECRETARIAT HAS REPORTED THAT INDUSTRIAL EXPORTS FOR THE FIRST HALF OF 1987 TOTALLED 766 MILLION DOLLARS, 11.2 PER CENT MORE THAN THE SAME PERIOD IN 1986. (CLARIN P20)

7. EXTERNAL

SOVIET FOREIGN MINISTER SCHEVARDNADZE IS TO VISIT BUENOS ARIES ON 30 SEPTEMBER. (AMBITO P1)

HEAD OF THE ARGENTINE INTERESTS SECTION IN LONDON, JUAN EDUARDO FLEMING, HAS MET FOREIGN MINISTER CAPUTO TO DISCUSS THE SITUATION IN POST-ELECTION BRITAIN WITH RESPECT TO THE FALKLAND

ISLANDS. (CLARIN P17)

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PRESS SUMMARY FOR 27 AUGUST

1. MAIN HEADLINES

STRIKES AND COLLECTIVE BARGAINING AGREEMENT.

2. LABOUR

TELEPHONE WORKERS HAVE ENDED THEIR STRIKE. THE DIRECTOR OF ENTEL, NICOLAS GALLO, HAS RESIGNED, TAKING RESPONSIBILITY FOR GRANTING WAGE INCREASES ESTIMATED AT BETWEEN 15 AND 60 PER CENT. (CLARIN P3, AMBITO P1)

ARGENTINE RAILWAYS REMAIN PARTIALLY PARALYZED BY STRIKES BUT GOVERNMENT EMPLOYEES AND AEROLINEAS ARGENTINAS PILOTS HAVE DECIDED AGAINST STRIKE ACTION. (CLARIN PP2/4/7)

LABOUR MINISTRY SOURCES HAVE DENIED THAT LABOUR MINISTER ALDERETE THREATENED TO RESIGN IN THE FACE OF A GOVERNMENT PROPOSAL TO HAVE TELECOMMUNICATIONS CENTRES TAKEN OVER BY THE GENDARMERIE NATIONALE OR THAT THE PROPOSAL WAS EVER CONSIDERED. (CLARIN P5)

THE DECREE DECLARING COLLECTIVE WAGE BARGAINING TALKS WITHOUT PRE-SET LIMITS IS TO BE ANNOUNCED TODAY. (PRENSA P1)

3. POLITICAL

RADICAL DEPUTY FEDERICO STORANI HAS PREDICTED THAT THE FORTHCOMING ELECTION WILL SEE A POLARISATION OF VOTES TO THE DETRIMENT OF SMALLER PARTIES. (CLARIN P10)

4. EXTERNAL

FOREIGN MINISTER DANTE CAPUTO HAS DESCRIBED RELATIONS WITH PARAGUAY AS DELICATE FOLLOWING THE PARAGUAYAN GOVERNMENT'S REFUSAL TO EXTRADITE TWO FORMER MEMBERS OF THE ARGENTINE SECURITY FORCES. ''AMBITO FINANCIERO'' CLAIMS THAT THE PRESENT COOLNESS IN RELATIONS WITH PARAGUAY IS A DELIBERATE ELECTORAL PLOY BY THE GOVERNMENT AIOED AT SECURING THE VOTES OF PARAGUAYAN EXILES RESIDENT IN ARGENTINA. (AMBITO P11)

FRENCH PRESIDENT FRANCOIS MITTERRAND IS TO VISIT ARGENTINA FROM 6 TO 10 OCTOBER. (CLARIN P19, AMBITO P10)

5. MILITARY

A MIRAGE 3 FIGHTER BELONGING TO THE 8TH AIR BRIGADE IN MORENO HAS CRASHED NEAR GUALEGUAYCHU KILLING THE PILOT. (NACION P6, PRENSA P6)

A SIGNED ARTICLE IN ''AMBITO FINANCIERO'' CLAIMS THAT ARMY CHIEF OF STAFF GENERAL CARIDI'S ATTEMPTS TO REASSERT THE CHAIN OF COMMAND WITHIN THE ARMY HAVE NOT BEEN SUCCESSFUL. REPRESENTATIVES OF THE RADICAL GOVERNMENT ARE ATTEMPTING TO SEEK AGREEMENT WITH THE MIDDLE RANKING OFFICERS, WHICH COULD RESULT AFTER THE FORTHCOMING ELECTION IN A CHANGE OF DEFENCE MINISTER AND THE ARMY HIGH COMMAND. (AMBITO P13)

6. ECONOMIC AND FINANCIAL

INDEC REPORTS THAT UNEMPLOYMENT AND UNDER-EMPLOYMENT IN ARGENTINA IN APRIL WERE 6 AND 8.2 PER CENT RESPECTIVELY. (AMBITO P6)

THE PARALLEL DOLLAR CLOSED ON 26 AUGUST AT 3.06 AUSTRALES AND UNREGULATED INTEREST RATES REMAINED AT 15 PER CENT PER MONTH. (AMBITO P1)

US DEPARTMENT OF COMMERCE STATISTICS SHOW THAT DIRECT US INVESTMENT IN ARGENTINA ROSE 10 PER CENT IN 1986 TO 2.864 BILLION DOLLARS. (AMBITO P10)

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GENERAL INDEX OF RETAIL PRICES : AUGUST 1987

The annual rate of inflation, as measured by the 12 month change in the retail prices index, was 4.4 per cent in August, the same as for July.

2. The overall level of prices was 0.3 per cent higher in August than in July, matching the increase recorded between the corresponding months last year. Prices for clothing and footwear were higher, following the ending of summer sales, and there were widespread but small increases among other items.

3. In September the 12-month rate is expected to fall to around 4¼ per cent; with an increase in the overall level of prices of around 1/3 per cent between August and September replacing, in the 12-month calculation, the larger increase of 0.5 per cent between the corresponding months last year.

Producer Prices

4. The August figures on producer prices will be published next Monday. The annual change in the prices index for home sales of manufactured products was 3.6 per cent in July, much the same as in the previous four months. However over these months prices in sectors other than food, drink and tobacco have been moving faster than the RPI and are therefore likely to lead to upward pressure on retail prices.

5. Prices for materials and fuels purchased by manufacturing industry were 8.3 per cent higher in July than a year ago. A further indication of an underlying upward pressure on retail prices.

Tax and Prices Index

6. The tax and prices index increased by 2.6 per cent in the year to August compared with 2.8 per cent recorded for July.

What is the fig ex mortgage interest payments?

C/EA1 say they calculate figure to be 3.7% - but to be confirmed by DE - will let you know if figure different

CR 10/9.

PS Past figs are as follows:-

Jan	3.7
Feb	3.7
Mar	3.8
April	3.6
May	3.8
June	3.5
July	3.7

Thanks

PERSONAL AND CONFIDENTIAL

International comparisons

7. The latest 12-month percentage changes in consumer prices in the main OECD countries and the averages for all EEC and OECD countries are as follows:-

	UK	FRANCE	FEDERAL GERMANY	ITALY	NETHER -LANDS	JAPAN	USA	CANADA	OECD Averages	EEC
1986										
Q1	4.9	3.6	0.7	7.6	1.2	1.6	3.1	4.2	3.8	4.4
Q2	2.8	2.4	-0.2	6.1	0.4	0.8	1.6	3.9	2.5	3.2
Q3	2.6	2.1	-0.4	5.4	-0.4	0.2	1.7	4.2	2.5	3.0
Q4	3.4	2.1	-1.1	4.4	-1.8	-0.5	1.3	4.3	2.1	2.9
1987										
Q1	3.9	3.2	-0.5	4.1	-1.2	-1.3	2.2	4.1	2.3	2.2
Q2	4.2	3.1	0.1	4.2	-1.0	-0.2	3.8	4.6	3.5	3.0
March	4.0	3.3	-0.2	4.2	-1.1	-0.8	3.0	4.2	3.0	3.0
April	4.2	3.5	0.1	4.3	-1.1	-0.2	3.8	4.5	3.5	3.1
May	4.1	3.4	0.2	4.2	-1.1	-0.3	3.8	4.7	3.4	3.1
June	4.2	3.3	0.2	4.4	4.4	..	3.7	4.8	3.4	3.1
July	4.4									
August	4.4									

Note: The July and August figures for the OECD countries are not available.

STATISTICS DIVISION
DEPARTMENT OF EMPLOYMENT 9th SETPEMBER 1987

PERSONAL AND CONFIDENTIAL UNTIL 11.30AM ON FRIDAY 11 SEPTEMBER 1987

184/87 September 11, 1987

GENERAL INDEX OF RETAIL PRICES

AUGUST 1987

The general index of retail prices for all items for August 11, 1987 was 102.1 (January 13, 1987 = 100). This represents an increase of 0.3 per cent on July 1987 (101.8) and an increase of 4.4 per cent on August 1986 (385.9, January 1974 = 100).

The rise in the index between July and August was the result of higher prices for clothing and footwear, with the end of summer sales, and widespread but small increases in the prices of a range of other items.

The movements for the main groups in the index are shown in Table 2.

Table 1.

	All items				All items except seasonal food		
	Index Jan 13 1987 = 100	Percentage change over 1 month	6 months	12 months	Index Jan 13 1987 = 100	Percentage change over 1 month	6 months
1987							
March	100.6	+0.2	+2.3	+4.0	100.6	+0.3	+2.3
April	101.8	+1.2	+3.4	+4.2	101.6	+1.0	+3.0
May	101.9	+0.1	+2.6	+4.1	101.7	+0.1	+2.2
June	101.9	+0.0	+2.3	+4.2	101.8	+0.1	+2.1
July	101.8	-0.1	+1.8	+4.4	101.9	+0.1	+1.9
August	102.1	+0.3	+1.7	+4.4	102.2	+0.3	+1.9

TABLE 2

	Indices (13 January 1987 = 100)		Percentage change
	July 14, 1987	August 11, 1987	over the month
All items	101.8	102.1	+0.3
All items excluding food	102.1	102.4	+0.3
All items excluding housing	101.4	101.7	+0.3
Food	100.4	100.7	+0.3
Seasonal food	97.0	98.6	+1.6
Non seasonal food	101.0	101.0	0.0
Catering	102.9	103.6	+0.7
Alcoholic drink	101.7	102.1	+0.4
Tobacco	99.7	99.5	-0.2
Housing	103.8	104.1	+0.3
Fuel and light	99.1	99.0	-0.1
Household goods	101.6	101.9	+0.3
Household Services	102.0	102.4	+0.4
Clothing and footwear	99.2	99.8	+0.6
Personal Goods and Services	101.9	102.4	+0.5
Motoring Expenditure	104.4	104.8	+0.4
Fares and Other Travel Costs	102.2	102.3	+0.1
Leisure Goods	101.6	101.7	+0.1
Leisure Services	101.4	101.4	0.0

NOTES TO EDITORS

1 The General Index of Retail Prices (RP1) measures the average change from month to month in the prices of goods and services purchased by most households in the United Kingdom. The expenditure pattern on which the index is based is revised each year using information from the Family Expenditure Survey. The expenditure of certain higher income households and pensioner households, mainly dependent on state pensions and benefits, is excluded.

2 The index is compiled using a large and representative selection of more than 600 separate goods and services for which price movements are regularly measured in about 180 towns throughout the country. Approximately 130,000 separate price quotations are used each month in compiling the index.

3 The prices of some items of food show significant seasonal variation. A separate price index is compiled for these "seasonal foods", the expenditure on which accounts for around 2½ per cent of household expenditure. The variation caused by these items is removed from the series of indices for 'all items except seasonal food'.

4 Rates of change of indices can be calculated over periods of any length. Rates calculated over long periods are slow to detect changes in trend while calculations over very short periods give rather volatile results. To help in assessing what is happening to prices, rates of changes in the all items index and the index for all items except seasonal food are shown in Table 1 over successive periods of one month, six months and twelve months.

5 Following the recommendations which the Retail Prices Index Advisory Committee made in its report submitted to the Secretary of State for Employment in July 1986, the index has been re-referenced to make January 1987 = 100. Calculations of movements in the index over periods of time which span January 1987 are made as follows:-

> The index for the later month (January 1987 = 100) is multiplied by the index for January 1987 (January 1974 = 100) and divided by the index for the earlier month (January 1974 = 100). 100 is subtracted to give the percentage change between the two months.
>
> Using the all items index for example: take the index for August 1987 (102.1) and multiply it by the January index (394.5) then divide by the August 1986 index (385.9). Subtract 100 from the result which gives 4.4 as the percentage change in the index over the twelve months to August.

6 The index for August 1987, if translated to the old reference date (January 1974 = 100) would be 402.8.

7 Other changes made to the index in 1987 are given in an article in the April edition of Employment Gazette.

8 The Retail Prices Index Advisory Committee was first established in 1946 and advises on the methodology used for compiling the RPI. Committee members include representatives of consumers, employees, employers, retailing organisations, academic experts, government departments and other official bodies. The Committee's latest report - 'Methodological Issues Affecting The Retail Prices Index' Cmnd 9848 HMSO £6.50 - was published on 15 July 1986. The Government announced at the same time that all its recommendations were to be accepted.

9 The housing costs of owner-occupiers are reflected in the index using an indicator which represents mortgage interest payments. A weighted average of building societies base mortgage interest rates is used in the calculation.

10 The index is given in full in the Employment Gazette.

MC

PERSONAL AND CONFIDENTIAL

SECRETARY OF STATE FOR EMPLOYMENT

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Switchboard 01-213 3000 GTN Code 213
Facsimile 01-213 5465 Telex 915564

David Norgrove Esq
Private Secretary
10 Downing Street
LONDON SW1

9 September 1987

Dear David,

RETAIL PRICE INDEX

... I enclose a copy of our note and draft press release on the Index of Retail Prices due to be released at 11.30 pm Friday 11 September.

Numbered copies also go to Alex Allan (Treasury), Sir Peter Middleton (Treasury), Timothy Walker (Trade and Industry), Rachel Passmore (CSO), John Footman (Bank of England), Chris Cloke (CO) and Sir Brian Hayes (Trade and Industry).

Sincerely

Beverley Evans

BEVERLEY EVANS
Private Secretary

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11 September 1987

TAX AND PRICE INDEX, AUGUST 1987

The Tax and Price Index (TPI) for August was 100.0 based on January 1987 = 100. Over the twelve months to August the increase in the TPI was 2.6 per cent, compared with an increase of 4.4 per cent in the Retail Prices Index (RPI).

TAX AND PRICE INDEX

	TPI (Jan 1978=100)	TPI (Jan 1987 = 100)	Percentage change in TPI over 12 months	Corresponding change in RPI
1986				
January	192.9		4.4	5.5
February	193.7		3.9	5.1
March	194.0		3.0	4.2
April	192.5		1.2	3.0
May	192.9		0.9	2.8
June	192.8		0.6	2.5
July	192.1		0.4	2.4
August	192.9		0.6	2.4
September	194.0		1.2	3.0
October	194.3		1.5	3.0
November	196.3		2.2	3.5
December	197.1		2.4	3.7
1987				
January	198.0	100.0	2.6	3.9
February		100.5	2.7	3.9
March		100.7	2.8	4.0
April		99.7	2.5	4.2
May		99.8	2.4	4.1
June		99.8	2.5	4.2
July		99.7	2.8	4.4
August		100.0	2.6	4.4

Notes to editors

1. The purpose and methodology of the TPI were described in an article in the August 1979 issue of Economic Trends, and the series from January 1979 is published regularly in the Monthly Digest of Statistics. Figures from January 1976 are available from the CSO.

What the TPI measures

2. The TPI measures the increase in gross taxable income needed to compensate taxpayers for any increase in retail prices. The RPI measures changes in retail prices; the TPI also takes account of the changes to direct taxes (and employees' National Insurance contributions) facing a representative cross-section of taxpayers. It is thus an additional, more comprehensive, index.

3. The TPI increased by 2.6 per cent over the twelve months up to August 1987 while the RPI increased by 4.4 per cent. The increase in the TPI was smaller because of the increase in personal income tax allowances and the reduction in the basic rate of income tax in the 1987 Budget. The effect on the TPI of the changes in National Insurance contributions, which took effect in April 1987, was negligible.

4. When direct taxation or employees' National Insurance contributions change (usually at Budget time) the TPI will rise by less than or more than the RPI according to the type of changes made. Between Budgets the monthly change in the TPI is normally slightly larger than that in the RPI (a more than proportionate increase in gross income is needed to offset any rise in prices, since all the extra income is fully taxed). In fact because of rounding both the RPI and the TPI rose by 0.3 per cent between July and August 1987. However, the focus of attention should be the changes over twelve months.

Coverage and calculation of the TPI

5. Non-taxpayers and those with incomes over £22,415 a year at January 1987 are excluded from the TPI. Non-taxpayers are excluded because the RPI already provides a measure of the change needed to maintain the purchasing power of their incomes. Those with high incomes are excluded because the changes in their tax liabilities are not necessarily representative of the majority of tax-payers, and because broadly the same percentage (the top 4 per cent) is already excluded from the households on whose expenditure patterns the RPI is based. Otherwise everybody is included, whether working, unemployed or retired, so long as they pay tax.

6. The TPI reflects changes in people's tax and National Insurance contribution liabilities. If the index were instead to reflect actual payments it would be subject to highly erratic movements, which would be difficult to interpret and could be misleading.

7. The current composition and distribution of gross taxable incomes are estimated from Inland Revenue's Survey of Personal Incomes in 1984/85, updated by later aggregate data on incomes. With the exception of housing benefit, non-taxable income, (and in particular child benefit), is not covered. From February 1987 onwards, housing benefit is included in the income base for calculating the TPI because of changes made to the RPI as a result of the RPI Advisory Committee's recommendations. The RPI now reflects changes in gross housing costs which, for a substantial minority of tax-payers, are partially offset by receipts of housing benefit. After excluding those with high incomes, the sample comprises 32,037 tax units (single people or married couples). The change in tax and National Insurance contribution liability resulting from any uniform increase in gross incomes can be estimated from this. So the change in gross income needed to offset a particular RPI increase can be found.

2328/12

PPS M.

8/7 18/8

FROM: N I HOLGATE

DATE: 4 August 1987

Pes in?

TL 6/8

1. MR HAWTIN

2. CHANCELLOR

cc Chief Secretary
Sir P Middleton
Mr F E R Butler
Mr Anson
Mr Gilmore
Mr Hawtin
Mr Turnbull
Mr Scholar
Mr Luce
Mr Potter
Mr Cropper
Mr Tyrie
PS/IR

I have drastically shortened, by omitting Mr Holgate's main objection to ~~the~~ Mr Ridley's proposed form of CC demand note. I have done so because Mr R used the importance of linking the CC to charge at spending relative to need as one of his main arguments against dual running. [illegible], However, better that him on dual running, we cannot use this argument against him. PS/ check that para 3, as amended, is correct. M.

DUAL RUNNING: RATES AND THE COMMUNITY CHARGE

Mr Ridley minuted the Prime Minister on 30 July about minimising the costs of the dual running of domestic rates and the Community Charge (CC) from 1990 to 1994 in England. (The Prime Minister's private secretary replied on 31 July that the Prime Minister was content, subject to the views of colleagues.) The minute discusses two largely separate issues: the running down of the domestic rating system and the presentation of the CC demand note.

2. We recommend that you support the proposals on running down the rating system; but we suggest you ask Mr Ridley to reconsider the form of the CC demand note.

The Rating System

3. Mr Ridley proposes to freeze the valuation list (which is based on the 1973 valuation) as it stands in 1990. Accordingly:

(a) occupiers of new property will not be assessed for rates but will pay an amount based on the average domestic rate payment for the area;

(b) improvements or extensions to existing property will not result in an increase in rateable value;

(c) most challenges to rateable value by householders will also be cut off; but those affected by a material change of circumstances will be able to seek a reduced valuation and will have a limited right of appeal;

(d) mandatory and discretionary reliefs will be unchanged; and

(e) the amount of the progressive decline in rate poundages over the transition period will be specified by order.

4. There are minor disadvantages to the proposals. The valuation list will not be kept up to date; that inevitably introduces inequity between ratepayers in similar size houses, between new and old and between those extended or up-graded and those not. But the resulting distortion to the housing market would be small in scale. Mr Ridley points to the boost to the building trade that the abandonment of rating of home improvements will provide. It may also cause a temporary fall in demand in the months before April 1990 as households postpone their plans for improvements. But again this is a minor distortion.

5. There is a major advantage in Mr Ridley's proposals - the release of resources in the Valuation Office (VO), otherwise tied up in maintaining the valuation list. Mr Ridley's proposals fall between the two options for savings which Mr Potter outlined in his submission to you of 21 July. Annual savings of about £12 million a year in running costs should therefore be secured at current prices after the backlog of appeals has been cleared.

6. The relatively minor distortions to the housing and construction markets, set against the resource gain and Exchequer savings from running down the VO, argue in favour of Mr Ridley's proposal.

7. We also judge that, despite Mr Ridley's assertion that the measures would not preserve a rating system capable of resuscitation at some future date, the preservation of the list would allow Ministers to extend the transition period if they so chose. As new property forms only about 2% of total hereditaments each year, a 'frozen' valuation list would take several years to become significantly out of date (and owners of new property will anyway be paying the average in domestic rates). There would therefore be some time in which it could be brought up to date or a replacement devised, if that was thought necessary. We therefore recommend you support these proposals.

Presentation

8. Mr Ridley's suggestion for the format of the CC demand note is shown in an Annex to his minute. It is drawn from that proposed in his paper E(LF)(87)26 on the new grant system and focusses on spending per adult. It deducts contributions from business and government and (in the transition) domestic ratepayers to show the CC payable.

9. We doubt whether a format designed for the operation of the PLG system can be used successfully in the transition period. It will add to the confusion and obscurity of the relationship between LA spending and assessed need on the one hand, and the individuals CC and residual rates bills on the other.

(a) The figure for domestic rates on the CC demand note will not correspond to the actual payments made by ratepayers, as it is only an average per adult. This may be confusing.

(b) The layout of the demand note shows the average domestic rates payment separately from the CC. It thereby fails to make clear the full contribution paid by local residents to LAs.

(c) Excessive attention will be focussed on the bottom line, the CC payable. This figure tells residents very little about spending relative to need. In 1990 the charge will simply show whether the authority is spending more or less in real terms than it did in 1989.

(d) Support for this form of demand note at E(LF) rested on the individual being able to link his CC to changes in spending relative to need. But this process will be obscured during the phasing out of the safety net and by the changing mix of domestic rates and community charges.

10. We believe that the format for demand notes in the transitional period needs reworking. CC payers will be unable to see a simple link between their bills and the numbers in the note. And they are unlikely to take accountability seriously

when the full PLG system is in place if their demand notes have concealed more than they have revealed for the previous four years.

11. There is one further objection to this format. It nets off specific grants from the figures for spending and for government grants. Officials have yet to find a way in which the full extent of the taxpayer's contribution can be made clear to local residents. We continue to press for their inclusion.

Conclusion

12. Mr Ridley's proposals for the rating system produce savings in the Valuation Office. There is little point in keeping the full system in perfect operation; and the option to extend the transition period is not, in practice, closed-off by Mr Ridley's proposals.

13. His suggestion for the format of the bill has several deficiencies. It places excessive weight on the CC payable and promises more than it can deliver on accountability because of the transition and the safety net.

14. A draft letter is attached.

N.I. Holgate.

N I HOLGATE

DRAFT LETTER TO:

The Rt Hon Nicholas Ridley AMICE MP
Secretary of State for the Environment
Department of the Environment
2 Marsham Street
LONDON
SW1P 3EB

DUAL RUNNING : RATES AND THE COMMUNITY CHARGE

Thank you for copying to me your minute of 30 July to the Prime Minister.

2. I am broadly content with your recommendations on the running down of the rating system. They will enable me to secure savings in the Valuation Office.

3. However, I do have some reservations about adapting the format planned for the full community charge demand note in the way you suggest for the transitional period, since it fails to give any indication of the contribution made by Government through specific grants. We clearly need a formulation which does show this.

(a) The figure for domestic rates on the community charge demand note will not correspond to individuals' actual payments, which may cause confusion among ratepayers.

(b) The layout of the note does not give an aggregate figure for residents' contributions to local government. Without such a figure, prominence is given to the charge payable. This may give a misleading impression about an authority's level of overspending. Authorities could cut their spending in 1990-91 while continuing to spend above need. This would produce a charge of less than £100 and suggest to chargepayers that the authority was making great progress in controlling its level of spending when in fact it could still be spending far too much.

(c) The charge from 1991-92 will be affected by the transition from rates and the phasing out of the safety net as well as by authorities' decisions on spending.

4. Altogether, I believe that we need to think further about the presentation of the demand note for charge payers during the transitional period. It may be best if we can find some form of interim format which makes greater allowance for the problems I have outlined, and then move to the format suggested in E(LF)(87)26 (with some indication of the contribution made by central government through specific grants) when the transition is over and full accountability is possible.

5. I am copying this letter to members of E(LF) and to Sir Robert Armstrong.

N.L.

CONFIDENTIAL

RD

CH/EXCHEQUER
REC. - 6 AUG 1987 6/8
ACTION CST
COPIES TO

SECRETARY OF STATE FOR THE ENVIRONMENT

Prime Minister

ROLE OF THE TREASURER

The purpose of this minute is to seek your agreement and that of E(LF) colleagues to my proposals, to be included in the Rate Reform Bill, to strengthen the position of a local authority treasurer in dealing with potential illegality and impropriety by his council. Colleagues will be aware of the proposal from discussion in MISC 109 and elsewhere. The details, on which Counsel has been instructed, were included in the first report of the official Working Group on Local Authority Financial Prudence which I circulated to colleagues with my letter of 25 June to John Major.

Background

The Green Paper "Paying for Local Government" proposed a specific statutory role for the Treasurer or Chief Finance Officer to strengthen his position in relation to the legality and propriety of the expenditure by his authority. Whilst this proposal was generally not well received by local government, I believe it will be an important factor in encouraging more prudential behaviour by local authorities.

The proposal

The scheme I have developed is with one exception as proposed in the Green Paper and as follows:

(a) the Chief Finance Officer would be required to hold a recognised professional qualification. Most already do and this is simply a slight tightening up to ensure against rogue appointments in the light of the new duties proposed below. Those Chief Finance Officers now in post, but without qualifications, would not be debarred.

(b) The Chief Officer would be under a duty

i to make a report to his authority in respect of any decision of the authority which would in his opinion involve the making of a payment contrary to law or in respect of any act or omission which would be likely to cause a loss or deficiency because of wilful misconduct.

ii to make a report to his authority if at any time the expenditure proposed to be undertaken by the authority in any financial year, together with the expenditure incurred already if any, would in his opinion be likely to exceed the resources available to the authority to finance their expenditure.

iii to send a copy of any report under (i) or (ii) above to the auditor.

(c) The authority receiving such a report is to be required to consider it at a meeting within 21 days, and not to make any payments in relation to the subject matter of the report until it has done so. The report should be public and the public allowed access to the meeting.

The main effect of the scheme therefore is to ensure that the Treasurer draws matters of illegality and impropriety to the attention of the council, its auditor and the public. The reports should provide one basis on which the auditor could issue a stop notice - using the narrower element of the powers proposed in my letter to the Lord President of 17 July. If a council considers a Treasurer's report and then proceeds with the action (or inaction) which it is aimed to deter, the reports would provide important evidence in any case for the surcharge/disqualification of the Councillors concerned.

SECRETARY OF STATE FOR THE ENVIRONMENT

The element of the original Green Paper proposal which I have set aside in this scheme is the requirement that the Treasurer certify the taxing resolution of his authority. I believe this would put too much strain on the relationship between the officer and his councillors, and that it is anyway unnecessary. If the proposed budget of an authority is out of balance this is something on which the Treasurer would be required to report. The auditor could then issue a stop notice because it is unlawful to budget for a deficit.

I should also note here that my proposed approach is inconsistent with Widdicombe's view that all functions related to the propriety of council business should be vested in the Chief Executive. I take the view that matters relating to financial propriety should be left with the professionally qualified Treasurer.

Conclusion

I would be grateful to know urgently whether you and colleagues are content with the approach I have adopted.

I am copying this to members of E(LF) and Sir Robert Armstrong.

R[illegible]

pp N R

5 August 1987

(Approved in draft by the Secretary of State and signed in his absence.)

CONFIDENTIAL

FROM: A G TYRIE

DATE; 4 AUGUST 1987

CHANCELLOR

cc Chief Secretary
Financial Secretary
Paymaster General
Economic Secretary
Mr Cropper
Mr Scholar
Mr Isaac
Mr Corlett
Mr Stewart

Re para 5, I sh'd have known in the context of the FST's 6(vi) that he is clearly well to point to the complex interaction (wh we will have to have in mind) between the ~~that~~ student covenant suggestion & the review of student support. What we really want is a coherent package for the covenant gone, "top-up" loans on the students, the parental contributions, ~~[illegible]~~ scholarships reduced, & aspiring grant students contribution before Sec of State ...

COVENANTING AND MAINTENANCE

You asked for comments.

2. I agree with the Financial Secretary on this. We need to act on Sherdley and to close the loophole created by independent taxation, but probably no more.

3. This is one area where I am a deviant on fiscal neutrality and I disagree with Mr Stewart's contention (in paragraph 33) that we should seek neutrality between divorced and married couples. Divorce is expensive and if there were no fiscal benefits we would have to substitute them with higher public spending. It is generally accepted that divorce settlements should relate to people's standard of living prior to divorce. It is arguable that the tax system is a better way of delivering this than public expenditure could be. In any case, the Revenue's estimated gain from their own proposal is very small. Is it worth the candle?

TYRIE TO CH/EX 4AUG

4. Only when large numbers of people start getting separated/divorced to obtain a fiscal advantage would further action be called for. I cannot believe we have arrived at this point.

5. As for students, convoluted though the system may

I sh'd be grateful if officials (Mr Burns?) cd work up a scheme I can put to Mr Baker. N.

be, I see advantages in the retention of convenanting. Alternatives are likely to weaken the link between the giver and the recipient. We would probably have to replace covenanting with increased public spending. Covenanting, although imperfect, is at least going down the right road for funding higher education. Nor am I a wholehearted supporter of action on grandparent covenanting.

AGT.

A G TYRIE

A/ I have not replied to this.
AA 11/8

-pvg

SECRETARY OF STATE FOR THE ENVIRONMENT

2 MARSHAM STREET
LONDON SW1P 3EB
01-212 3434

My ref:

Your ref:

CH/EXCHEQUER
REC. -7 AUG 1987
ACTION CST
COPIES TO

Alex Allan Esq
Private Secretary to
The Rt Hon Nigel Lawson MP
Chancellor of the Exchequer
HM Treasury
Parliament Street
SW1P 3AG

5 August 1987

Dear Alex,

PRESS NOTICE ON PHASING THE COMMUNITY CHARGE

Many thanks for your letter of 31 July. I am advised, however, that the description in it of the events on 30 July is so inaccurate and unfair that I must not let it go unanswered.

As you know, unlike you, me, or Jill, Mr Howard and Chris Brearley did attend the E(LF) meeting that morning. They re-drafted the Press Notice in the light of the comments made there, and I understand Chris Brearley read the revised version over to Robin Fellget at about 1.20 pm. We understood, and understand now, that that was in line with the Chief Secretary's request that the revised Press Notice should be cleared by one of his officials. The only Treasury amendment suggested then was to one word in the note to editors, which I gather we were glad to make.

After that telephone discussion, and after we had made that one amendment, Jill or someone from her office rang to ask for a copy of the draft to be faxed to them. We did this, I gather, at about 2.05 pm. This does seem a bit late, given that we were planning to release it to the Press at 2.30 pm, but we were proceeding on the basis that we had done as the Chief Secretary had asked in clearing the draft with his officials. When Jill phoned Neil Kinghan at about 2.30 pm, Neil checked with out Press Office what the position was and told Jill that it was indeed too late to take comments, because copies were being handed to the Press even as they were speaking. The Press were briefed by our officials at 2.30 pm, before Mr Howard saw the at 2.45 pm.

I set out these fascinating events in such enthralling detail only in order to correct the impression that I think you may have that we here deliberately over-rode your comments on the draft. I understand that was just not so. On the specific point about the references to national taxation in the Press Notice, both Mr Howard and Chris Brearley were adamant that the wording in the Notice should be used because the Prime Minister herself had made it absolutely clear at E(LF) that she wanted them to be used both on this occasion and in all other publications and pronouncements on the community charge.

When we spoke on the telephone you mentioned your worry that Treasury officials were unhappy with the statement that those on the top 10% of incomes contribute 20 times as much as those in the bottom 10% - not, I hope, because it is not true now, but rather because it may well not be true in 1990. Given the Prime Minister's attraction to the line of argument and the very frequent airing which both we and the Scots have given it, I am not sure how you want to pursue your objection. If it is a matter of careful wording, perhaps this is something our officials can agree on between them.

As you say, we must certainly ensure that we try to do better in agreeing on the terms of Press Notices affecting our 2 Departments in future.

I am copying this letter to Jill Rutter in the Chief Secretary's office, but let us declare peace over spilt milk!

Yours,

R U YOUNG
Private Secretary

Robin.

psl/53A

RESTRICTED

cc PS/Chief Secretary
Sir P Middleton
Mr Culpin
Mr Potter

Treasury Chambers, Parliament Street, SW1P 3AG
01-270 3000

pwy

31 July 1987

Robin Young Esq
PS/Secretary of State for the Environment
Department of the Environment
2 Marsham Street
LONDON
SW1P 3EB

Dear Robin

PRESS NOTICE ON PHASING THE COMMUNITY CHARGE

As I told you on the phone, we were most unhappy about the way the clearance of this afternoon's press notice was handled. At E(LF) this morning it was agreed that the press notice should be cleared with the Chief Secretary. We assembled comments on the version handed round at E(LF), but were told that a revised version was being prepared and would be faxed over to us.

After much pressing, the revised version was finally faxed to us at 2.15 pm. It contained several new passages, including some about taxation which are clearly the Treasury's responsibility. Jill Rutter 'phoned Neil Kinghan at 2.30 pm to pass on some comments, including one on taxation that we felt particularly strongly about, only to be told that the final versions had been run-off. She insisted that they be held while we checked one point with David Norgrove and with the Chief Secretary.

I did this, and rang Neil Kinghan back at 2.45 pm, to press a new form of words on taxation, to be told that the press notice had already been issued.

The press notice was thus issued without being cleared with Treasury Ministers, in spite of known Treasury objections on subjects within our responsibility. I trust you will make sure this does not happen again. I am sure you would feel just as concerned if the circumstances were reversed, and it was the Treasury issuing a press notice without proper clearance with DOE.

Yours
Alex

A C S ALLAN
Principal Private Secretary

2328/13

CONFIDENTIAL

FROM: N I HOLGATE

DATE: 10 August 1987

1. MR HAWTIN

2. CHANCELLOR

cc PS/Chief Secretary
Mr F E R Butler o/r
Mr Potter o/r
Mr R P Short o/r

COMMUNITY CHARGE

Mr Allan's minute of 5 August asked about the determination of the initial community charge and about DOE statistics on the contribution of those with high and low incomes in national taxes.

The Initial Community Charge

2. Mr Ridley's third E(LF) paper on introducing the charge E(LF)(87)35, recommended that there should be an initial charge of £100 for those local authorities which spent the same in real terms in 1990-91 as they had done in 1989-90.

3. The DOE Press Notice of 30 July was slightly more vague. It said that the charge should be £100 everywhere "if authorities spend the same amount in 1990 as in 1989".

4. Altogether three DOE intentions are relevant to determining the likely CCs in the transition:

(i) A £100 community charge for unchanged real spending.

(ii) A safety net which ensures that the domestic tax bill (rates and the charge) will be the same in real terms in 1990-91 as it was in 1989-90.

(iii) The phasing out of domestic rates in equal cash amounts between 1990-91 and 1994-95.

These assumptions together with the indexing of non-domestic rates imply that the grant percentage for spending the same in real terms in 1989-90 and 1990-91 will be stable.)

5. Together these will amplify the gearing effect of LAs' increases in real spending on the community charge. Thus the average authority may raise about 10% of its total revenue from the community charge in 1990-91 if it spent the same in real terms as it did the previous year. But if it increases its real spending by 3%, the entire overspend will be met through the community charge, implying an average charge in practice of £130.

6. Mr Ridley exemplified the transition for five sample authorities. If those authorities increased their (current) spending at the same rate in 1990-91 as they did in 1987-88, their charges would probably be between about £115 (Barnsley) and £145 (Camden). (The Camden charge is high because the charge in 1990-91 meets a comparatively small proportion of the borough's revenue, not because the rate of increase in spending is high.)

7. In the second and third years of transition, inflation will exacerbate the proportionate increases in the charge. As domestic rates will be scheduled to fall in equal cash amounts, inflationary increases for the whole of residents' contributions will be concentrated on the charge.

8. Given the DOE intentions, the payment of extra grant in 1990 would not reduce the initial community charge. It would merely reduce the residual domestic rates to be levied.

Contributions in national taxation

9. DOE's source for their statistic is a figure culled by the Scottish Office from the annual article in Economic Trends on the effects of taxes and benefits on household income. I attach a copy of a table from the most recent article.

10. Apparently the payments of income tax, national insurance, VAT and other indirect taxes on final goods and services were

added up for the top and for the bottom decile points of households. Rates were then deducted. This produced a contribution from the top decile point 19.9 times larger than that of the bottom decile point. The addition of an estimate of the community charge produced a figure for the top decile's contribution that was 18.8 times larger than that of the bottom one. These calculations were "rounded up" to 20.

11. I believe that Mr Short used the most up to date article, included tax relief at source and intermediate taxes (which DOE did not), excluded rates and made no assumption about the community charge. This yields a multiple of 15.4.

12. The DOE statistic therefore appears to be rounded, slightly out of date and more selective in the taxes included than the Treasury calculation.

N I Holgate

N I HOLGATE

Average incomes, taxes and benefits, 1985

By decile groups of households ranked by original income

TABLE 5

£ per year

	Decile group										Average over all decile groups
	1st	2nd	3rd	4th	5th	6th	7th	8th	9th	10th	
Decile points (£)	*20*	*620*	*2 487*	*5 464*	*7 802*	*9 970*	*12 289*	*15 079*	*19 698*		
Number of households in the sample	701	701	702	701	701	701	701	702	701	701	7 012
Original income											
Earnings of main earner	-	30	358	2 244	5 069	6 993	8 334	9 581	11 373	17 598	6 158
Other earnings	-	-	13	126	412	894	1 895	3 062	4 524	7 746	1 867
Occupational pensions, annuities	-	98	621	1 086	674	499	442	429	509	625	498
Investment income	1	88	327	438	386	369	362	489	623	1 339	442
Other income	-	26	65	174	154	119	77	105	96	217	103
Total	1	242	1 384	4 067	6 695	8 872	11 109	13 666	17 125	27 526	9 068
Direct benefits in cash											
Contributory											
Retirement pension	1 054	1 643	1 797	1 029	448	291	182	207	183	129	696
Unemployment benefit	47	64	82	108	88	80	50	41	35	30	62
Invalidity pension and allowance	136	154	172	146	111	45	30	12	19	5	83
Statutory sick pay	-	1	2	18	25	25	26	31	31	29	19
Industrial injury disablement benefit	9	28	19	42	7	14	3	9	8	3	14
Sickness, industrial injury benefit	16	18	9	14	18	11	8	6	8	5	11
Widows' benefit	58	47	78	72	66	41	34	21	22	9	45
Maternity allowance	4	1	2	4	14	24	13	10	6	3	8
Christmas bonus for pensioners, etc	7	10	11	6	3	2	1	1	1	1	4
Other contributory benefits	8	14	21	18	14	-	3	2	3	2	9
Non-contributory											
Supplementary benefit	1 046	423	234	256	135	98	43	34	70	37	238
Child benefit	217	99	96	188	263	301	324	308	271	264	233
Rent rebates and allowances	657	371	180	128	44	20	13	-	2	2	142
Attendance allowance	47	33	28	29	18	13	8	5	8	11	20
Mobility allowance	35	25	21	24	21	8	9	7	12	8	17
War pensions	10	13	32	14	12	14	8	-	6	7	11
Severe disablement allowance	55	51	34	37	17	11	19	12	18	7	26
Student maintenance awards	17	20	42	35	18	6	12	10	21	14	20
TOPS/YTS, etc, awards	15	10	13	20	24	20	28	24	25	20	20
Family income supplement	2	5	6	28	8	1	4	1	1	2	6
Other non-contributory benefits	11	32	31	20	15	4	8	3	3	2	13
Total	3 452	3 062	2 910	2 235	1 369	1 029	828	744	753	590	1 697
Gross income	3 454	3 303	4 293	6 303	8 064	9 901	11 937	14 410	17 878	28 116	10 765
Income tax and Employees' NIC											
Income tax	1	14	136	492	947	1 365	1 814	2 370	3 161	5 897	1 620
Employees' national insurance contributions	-	2	16	155	395	568	709	880	1 062	1 381	517
less: Tax relief at source[1]	15	21	27	56	144	221	292	354	390	510	203
Total	-14	-4	125	592	1 198	1 713	2 230	2 896	3 833	6 768	1 934
Disposable income	3 468	3 307	4 168	5 711	6 865	8 188	9 707	11 514	14 045	21 347	8 832
Indirect taxes											
Domestic rates[2]	95	144	255	309	347	370	394	442	468	573	340
Taxes on final goods and services											
VAT	204	195	294	457	508	646	743	886	1 055	1 521	651
Duty on tobacco	179	110	128	187	205	228	220	207	225	243	193
Duty on beer and cider	29	21	35	62	74	100	103	125	139	182	87
Duty on wines	4	5	8	15	18	20	28	34	52	88	27
Duty on spirits	15	21	36	53	47	61	60	88	97	146	62
Duty on hydrocarbon oils	22	24	47	86	104	141	156	203	236	310	133
Car tax	3	2	6	13	15	24	27	34	43	67	23
Vehicle excise duty	11	16	31	49	57	71	77	91	105	133	64
Television licences	29	35	39	40	41	45	45	46	47	48	41
Stamp duty on house purchase	1	1	3	4	7	9	11	18	22	30	11
Customs' duties	12	11	14	22	24	30	33	40	47	62	29
Betting taxes	15	13	34	23	32	45	39	41	36	54	33
Other	12	11	11	14	16	17	18	24	25	29	18
Intermediate taxes											
Commercial and industrial rates	53	56	73	100	110	131	147	172	202	288	133
Employers' NI contributions	60	63	84	115	129	153	173	202	237	340	156
Duty on hydrocarbon oils	28	28	36	49	55	63	72	83	96	136	65
Vehicle excise duty	7	7	10	13	15	17	20	23	27	39	18
Other	24	26	35	47	53	63	71	82	95	134	63
Total indirect taxes	800	789	1 181	1 657	1 859	2 232	2 435	2 841	3 254	4 421	2 147
Income after cash benefits and all taxes	2 667	2 519	2 987	4 054	5 006	5 956	7 272	8 673	10 791	16 926	6 685
Benefits in kind											
Education	411	238	305	555	519	650	747	654	766	756	560
National health service	782	852	856	736	702	719	670	656	655	695	732
Housing subsidy	158	104	77	73	59	60	49	34	26	14	65
Rail travel subsidy	8	7	14	27	26	35	42	35	61	108	36
Bus travel subsidy	37	40	48	35	31	26	26	28	29	37	34
Welfare foods	75	30	25	41	25	22	19	18	17	14	28
Total	1 470	1 270	1 325	1 466	1 362	1 512	1 553	1 424	1 553	1 624	1 456
Final income	4 138	3 789	4 312	5 520	6 368	7 468	8 825	10 097	12 344	18 550	8 141

1 On mortgage interest and life assurance premiums.
2 Net of the rate rebate element of housing benefit, but including water, etc. charges.

CONFIDENTIAL

3

SECRETARY OF STATE FOR EDUCATION AND SCIENCE

ELIZABETH HOUSE
YORK ROAD
LONDON SE1 7PH
01-934 9000

CH/EXCHEQUER
REC. 10 AUG 1987 10/8
ACTION CST
COPIES TO

The Rt Hon Nicholas Ridley MP
Secretary of State for the Environment
Department of the Environment
2 Marsham Street
London SW1P 3EB

10 August 1987

Dear Nick,

RECOVERING THE COSTS OF GRANT-MAINTAINED SCHOOLS

Thank you for copying to me your minute of 30 July to the Prime Minister.

I understand the reasons why you are suggesting that the grant recovery should be achieved through a deduction from the needs assessment. However this method is not without difficulty. We would need to defend an approach in which the needs assessment was built up on one assumption about need to spend on GM schools but abated for the cost of those schools on another. The difference in the case, for example, of an ILEA school costing substantially more than GRE could be very difficult to defend. It would also have the effect of reducing the needs assessment for schools remaining with the authority, which would be presentationally very undesirable. It would mean that the relationship between the authority's expenditure and need changed (in percentage terms) because of a school opting out. There could also be difficulties over timing. I would expect opting out normally to take effect at the start of the academic year in September. But it will be desirable to fix the needs assessment at settlement in the previous autumn; it is unlikely that we will know so far in advance which schools will opt out and their associated costs.

I would therefore prefer a solution which left the needs assessment unchanged and reduced the authority's grant, after the latter had been determined on normal principles. It seems to me that the accountability problems which you describe could be overcome by including on the community charge bill the expenditure on GM schools in the area. I attach an example. My officials are discussing with yours an equivalent arrangement which might be applied in the existing rate support grant regime.

CONFIDENTIAL

The approach I propose would make clear to residents in the area that they will be financing GM schools on the same basis as LEA maintained schools. I do not see any problem in this. My consultation paper makes clear that the arrangements are intended to be financially neutral as between national and local taxpayers. I hope you will be able to accept this alternative arrangement.

I am copying this letter to the Prime Minister, to members of E(EP), and to Sir Robert Armstrong.

Yours ever

Kenneth

CONFIDENTIAL

SUGGESTED ALTERNATIVE FORM OF THE COMMUNITY CHARGE BILL

LEA with GM schools costing £50 per adult. Costs recovered by deduction of grant; needs assessment unchanged.

	£ per head	Actual spending		Standard Spending
Expenditure to be financed				
LEA expenditure		550		
GM schools		50		
		600		500
NDR income	233		233	
RSG	39		) 89	
Grant to GM schools	50		)	
	- 322	- 322	- 322	- 322
Community Charge		278		178

Andrew
PWP

From: Paul Davis
Date: 10 August 1987

PS / Economic Secretary
APS / Chancellor

cc PS/ Chancellor
PS/ Chief Secretary
Sir P. Middleton
Sir G. Littler
Sir T. Burns
Mr Cassell
Mr Sedgwick o/r
Mr Peretz
Mr Kelly
Miss O'Mara
Mr Culpin
Mr Davies
Mr Barrell o/r
Mr Owen o/r

June Trade Figures.

I attach a revised press briefing including the Chancellor's and Economic Secretary's comments in your minutes earlier today, and our subsequent conversation (Mr Barnes).

Paul Davis.

EA2 3SA/3 x 5384

DRAFT BRIEFING FOR IDT

Positive

Current account improved by £359 million in June as a result of sharp fall in imports compared with May. Monthly figures erratic but deficit of £168 million in June still leaves current account in surplus for first half of 1987, and £1384 million better than in second half of 1986.

2. CBI Survey for July shows export order books still buoyant.

3. Export volumes (excluding oil and erratics) in second quarter 6 per cent higher than a year earlier - stronger growth than in most other developed countries.

4. Terms of trade (both including and excluding oil) in second quarter improved by 3 per cent over previous quarter.

Defensive

1. Current account still in deficit. Current account deficit (of £2½ billion) forecast at time of Budget. Deficit only to be expected when UK growth running above long-term trend and rest of world growth below long-term trend. But May deficit shown to be freak: deficit reduced by £359 million. Current account in small surplus for year so far, which suggests overall deficit for 1987 below Budget forecast.

2. Strong domestic demand growth sucking in imports: Intermediate goods and semi-manufactures continue to make a large contribution to rise in imports, reflecting expansion of UK industrial activity.

3 Trend in imports upwards: Recent figures very erratic. Imports volumes (excluding oil and erratics) still below high level reached at end of last year. Due to volatility of recent figures, difficult to assess underlying trend.

Imports rising faster than exports [In second quarter on a year earlier, import volumes (excluding oil and erratics) up 9½ per cent, compared with 6 per cent rise for exports. On previous quarter import volumes up 5½ per cent while exports down 1½ per cent.] Not surprising given that UK economy is growing faster than most other major economies but exports likely to benefit from further improvements in world demand and UK's good competitive position.

5. Anticipated in Budget Forecast. FSBR forecast predicted 8 per cent rise in import volume (excluding oil and erratics) in 1987. So far this year 7 per cent up on 1986. Gains in competitiveness since end 1985 should help to restrain import growth and boost exports.

6. Capacity constraint threatens current account performance. [Phillips and Drew forecast 2 July 1987 stated export boom unlikely to last as competitiveness declines and imports likely to increase since industry facing capacity constraint. Reported by Philip Stevens, Financial Times 6 July.] Always expected imports to rise as economy grows strongly. Evidence of capacity constraints not conclusive. Industrialists report capacity utilisation relatively little changed over past year and still below 1973. CBI in latest survey state "there is no evidence of widespread bottlenecks due to fixed capacity over the next twelve months" with capacity utilisation little changed over past year. Moreover significant part of import rise is intermediate goods and semi-manufactures for expanding industry.

7 Exports no longer growing. In second quarter, export volumes (excluding oil and erratics) 6 per cent higher than same period a year ago. Volume of manufactures exports 4½ per cent up over same period.

8. Industry Act forecast for growth in exports in 1987 too optimistic: Exports forecast to grow in 1987 as world trade rises and benefits of improved competitiveness continue to come through. Latest CBI survey show export orders still buoyant. Export volumes (excluding oil and erratics) 6 per cent higher in second quarter than a year ago.

FSBR forecast of £2½ billion current account deficit in 1987 too optimistic: Current account of balance of payments shows small surplus in first half of this year.

10. Non-oil tradeable sector unable to respond owing to erosion of manufacturing base. [FT report on car components industry 30 June indicates many suppliers have disappeared although there is now some optimism following sterling's depreciation. Optimistic outlook corroborated in Commons Trade and Industry select committee report on UK motor components industry]. Manufacturing industry doing very well - output up 4½ per cent comparing latest three months with a year earlier. CBI surveys consistently optimistic. Volume of manufacturing exports (excluding erratics) 4½ per cent higher in second quarter than a year earlier.

11. Fall in exchange rate needed - sterling's recent strength threatens competitiveness: Non-oil visible trade responding to 1986 exchange rate adjustment. Period of stability in exchange rate desirable. Vital that pay settlements kept under control if existing gains in competitiveness to be maintained and endorsed by CBI.

12. UK's external position precarious: Current account in surplus in first half of 1987. FSBR forecast of current account deficit for 1987 only ½ per cent of GDP, following cumulative current account surplus of almost £20 billion between 1979 and 1986. With net overseas assets thought to be worth around £110 billion by end 1986, overall external position in any case strong.

SECRET AND PERSONAL

Pursued (I have just minuted.)

FROM: P D P BARNES
DATE: 10 August 1987

PLP

MR P DAVIS

cc PS/Chancellor
PS/Chief Secretary
Sir P Middleton
Sir G Littler
Sir T Burns
Mr Cassell
Mr Sedgwick
Mr Peretz
Mr Kelly
Miss O'Mara
Mr Culpin
Mr PJ Davies
Mr Barrell
Mr Owen

JUNE TRADE FIGURES

The Economic Secretary was grateful for your submission of 7 August.

2. The Economic Secretary had the following comments on a draft press briefing:-

(i) In Positive 1, add "compared with May" to end of first sentence.

(ii) In Defensive 1, add at end, "reduction in oil surplus due to expected North Sea summer maintenance shut down."

(iii) In Defensive 2, revise last sentence to read, "intermediate goods and semi-manufactures continue to make a large contribution to rise in imports, reflecting expansion of UK industrial activities."

(iv) In Defensive 3, revise last sentence to read, "too soon to quantify underlying trends."

(v) In Defensive 5, place second and third unbracketed sentences under new sub heading entitled "Anticipated in Budget Forceast". Insert new sentence between these two, "so far this year 7 per cent up on 1986".

(vi) In Defensive 9, the second sentence in square brackets should make clear what was corroborated.

PB

P D P BARNES
Private Secretary

PH1/87

SECRET AND PERSONAL
UNTIL 11.30 am TUESDAY 11 AUGUST
THEN CONFIDENTIAL

FROM: A P HUDSON
DATE: 10 AUGUST 1987

MR P J DAVIS

cc PS/Chief Secretary
PS/Economic Secretary
Sir P Middleton
Sir G Littler
Sir T Burns
Mr Cassell
Mr Sedgwick
Mr Peretz
Mr Kelly
Miss O'Mara
Mr Culpin
Mr Barrell
Mr Owen
Mr Norgrove - No.10

JUNE TRADE FIGURES

The Chancellor has the following comments on the press briefing attached to your 7 August minute.

a. Delete Positive 4.

b. Redraft Defensive 1 to read "Current account deficit (of £2½ billion) forecast at time of Budget. Deficit only to be expected when UK growth running above long-term trend and rest of world growth below long-term trend. But May deficit shown to be freak: deficit reduced by £359 billion in June and deficit on manufactures reduced by £391 million. Current account in small surplus for year so far, which suggests overall deficit for 1987 below Budget forecast.

c. Defensive 2, delete first sentence (now covered in Defensive 1).

d. Redraft Defensive 5 to read "CBI in latest survey state "there is no evidence of widespread bottlenecks due to fixed capacity over the next 12 months ", with capacity utilisation little changed over past year. Moreover significant part of import rise is intermediate goods and semi-manufactures for expanding industry".

e. Defensive 9 - replace first two sentences with "Manufacturing industry doing very well - output up 4½% comparing latest three months with a year earlier. CBI surveys consistently optimistic." In the final sentence, should the figure for manufacturing exports be 4½%?

f. Defensive 10 - at the end of the second sentence, add "and endorsed by CBI."

g. Defensive 11 - replace "some £19 billion" with "almost £20 billion."

AH

A P HUDSON

SECRET AND PERSONAL
UNTIL 11.30 am TUESDAY 11 AUGUST
THEN CONFIDENTIAL

FROM: PAUL DAVIS
DATE: 7 AUGUST 1987

1. ~~MR DAVIES~~ Approved in draft.
2. ECONOMIC SECRETARY

cc: See attached list

C. Press briefing OK?
OK as substantially amended. AH

JUNE TRADE FIGURES

The June trade figures will be published at 11.30 am on Tuesday 11 August. They will show a deficit on visible trade of £768 million. Combined with an unchanged CSO projection of the monthly invisibles surplus of £600 million, they give a projected current account deficit of £168 million in June compared to a revised deficit of £527 million in May. In the second quarter of 1987 the current account was in deficit by £630 million compared to a surplus of £667 million in the previous quarter. Small adjustments to the April and May current account figures have been made to take account of unprocessed documents resulting from the Customs strike. A similar adjustment has been made to the June figures which has the effect of reducing the current account deficit by £37 million.

Main points

2. **Current Account**

£ million

	1986 Year	Q3	Q4	1987 Q1	Q2	Apr	May	June
Manufactures	-5397	-1739	-1788	- 736	-1873	- 441	- 912	- 521
Oil	4153	646	846	1164	1022	419	361	242
Other goods	-7009	-1780	-1660	-1563	-1579	- 514	- 576	- 489
Total visibles	-8253	-2873	-2602	-1135	-2430	- 536	-1127	- 768
Invisibles	8133	2111	2017	1802	1800	600*	600*	600*
Current balance	- 120	- 762	- 583	667	- 630*	64*	- 527*	- 168*

* projection

3. The value of exports rose slightly between May and June, while imports fell by about £0.3 billion; hence the visible deficit in June was about £0.4 billion less than in May. In the second quarter of 1987 the visible deficit was £1.3 billion larger than in the previous quarter reflecting a £1.2 billion deterioration in the non oil

balance and a £0.1 billion fall in the oil surplus. Over the same period the manufacturing trade deficit widened by around £1.1 billion - to £1.9 billion - a little greater than the quarterly deficits in the second half of last year.

4. Exports

	percentage change			
	June on May	1987Q2 on previous quarter	1987Q2 on on same period year earlier	1986 on 1985
Total value	½	1½	8½	-6½
Total value excl. oil and erratics	½	0	9½	2½
Total volume	- ½	-3	3½	3½
Total volume excl. oil and erratics	½	-1½	6	2½
Manufactures volume (excl.erratics, OTS basis)	1	-1	4½	1
Fuels volume (OTS)	-7	-7	0	2
Basic materials volume (OTS)	13½	-17	17½	10½
Food, drink and tobacco volume (OTS)	- 5½	-3½	4	8½

5. Export volumes, excluding oil and erratics, rose by ½ per cent in June. Fuel exports fell by 7 per cent associated with an anticipated fall in North Sea production due to annual maintenance and there was a fall in food, drink, and tobacco exports of 5½ per cent. Basic materials exports rose in June, recovering most of the fall in the previous month.

6. In the second quarter export volumes (excluding oil and erratics) were 1½ per cent lower than in the previous quarter but 6 per cent higher than a year earlier. Within the total there were substantial falls from the last quarter in exports of basic materials and food, drink, and tobacco (the former due to the ending of the

olive oil trade, and the latter because of reduced disposals of excess grain stocks. The volume of manufacturing exports (excluding erratics) fell by about 1 per cent in the latest quarter. With little change in the export volume figures this month, the underlying level probably remains a little below the very high level reached at the end of last year, though it is still too early to say whether this is more than a pause in the longer term upward trend.

7. Imports

percentage change

	June on May	1987Q2 on previous quarter	1987Q2 on same period year earlier	1986 on 1985
Total value	-4½	4½	12	1
Total value excl. oil and erratics	-6½	4½	13	7
Total volume	-3½	5½	9	6½
Total volume excl. oil and erratics	-6½	5½	9½	6
Manufactures volume (excl.erratics, OTS basis)	-6	8	10	5½
Fuels volume (OTS)	33½	- 1	4	8½
Basic materials volume (OTS)	- 1½	½	16	6½
Food, drink and tobacco volume (OTS)	-14½	- ½	0	8

8. Import volumes, excluding oil and erratics, fell by 6½ per cent in June, reversing about two thirds of last month's rise. Imports of manufactures, basic materials and food, drink and tobacco fell. Within manufactures most categories fell though imports of passenger motor cars continued to rise from the low level in the first quarter. Imports of fuels rose in June roughly offsetting the fall in May (this again may reflect the fall off in production of North Sea oil in June as maintenance on installations takes place).

9. In the second quarter import volumes (excluding oil and erratics) were 5½ per cent higher than in the previous quarter, and 9½ per cent higher than a year earlier. Within the total, imports of manufactures continued to rise. Imports of semi-manufactures and intermediate goods continue to make a large contribution to recent growth, but the largest rise recordedwas for passenger cars (up 18 per cent on the previous quarter). There was little change in the remaining broad categories. Recent figures have been so erratic that the underlying trend is hard to discern. Although imports in the first half of 1987 have been a little below the high level in the last quarter of 1986, strong growth in most categories of manufactures seems to have resumed in recent months.

Geographical area

10. The value of exports to the US has been declining and in the second quarter was 24 per cent lower than in the previous quarter. Exports to the EC rose by 5 per cent and exports to Japan by 1 per cent. Exports to oil exporters fell by ½ per cent.

Trade prices

percentage change

	Import prices (OTS)		Export prices (OTS)	
	June on May	1987Q2 on previous quarter	June on May	1987Q2 on previous quarter
Manufactures (excl.erratics)	- ½	-2	0	1
Food, drink, tobacco	0	-2	½	-1
Basic materials	0	0	½	½
Fuel	2	-1	3½	-1
Total (BOP basis)	0	-2½	½	½
Total less oil(BoP basis)	- ½	-2½	½	½

11. In the second quarter the total terms of trade and the non-oil terms of trade as measured by unit value indices both improved by 3 per cent compared to the previous quarter. The favourable trend over the past few months reflects rises in the oil price and the exchange rate, only partly offset by rises in commodity prices in SDR terms. [NB: the published series are unit value indices, which can present a misleading picture over a period of time due to their use of 1980 weights.]

Comparison with the FSBR Forecast

12. In 1987 so far import volumes have been around 7 per cent higher than in the same period a year ago, compared with an FSBR forecast of 8 per cent growth for this year as a whole. The erratic path of imports recently makes it unusually hard to assess the underlying trend. But with all categories of manufactures imports now higher in the latest quarter than the previous quarter the figures indicate imports rising back towards the levels anticipated in the FSBR forecast after the low numbers at the start of the year, and we expect a rising trend in volumes through 1987. The FSBR forecast anticipated some fall in the volume of exports in early 1987, reflecting a projected fall in exports of non manufactures from the exceptional levels at the end of 1986. Whilst the fall in non manufactures has been close to what was expected, exports of manufactures have been weaker than expected. Nevertheless the manufacturing trade deficit, which was £2.6 billion in the first half of the year, would need to run at well above the June level in the second half of the year for the FSBR projection of £8 billion for the year as a whole to be exceeded.

Market expectations

13. The market expectation is for a current account deficit in the range £100-200 million in June (there are no revisions to invisibles forecasts). The June figures are broadly as expected, and should not be received badly by the City. Indeed, given the speculation in some quarters that Thursday's rise in interest rates heralds the announcement of bad trade figures on Tuesday, the City may be quite relieved that the deficit is below £200 million.

Press briefing

14. I would be grateful for clearance of the attached press briefing.

PAUL DAVIS
EA2

SECRET AND PERSONAL
UNTIL 11.30 am TUESDAY 11 AUGUST
THEN UNCLASSIFIED

DRAFT BRIEFING FOR IDT

Positive

1. Current account improved by £359 million in June as a result of sharp fall in imports. Monthly figures erratic but deficit of £168 million in June still leaves current account in surplus for first half of 1987, and £1384 million better than in second half of 1986.

2. CBI Survey for July shows export order books still buoyant.

3. Export volumes (excluding oil and erratics) in second quarter 6 per cent higher than a year earlier - stronger growth than in most other developed countries.

Difficult to put as a positive point this month, with passenger car imports up 18% Q2 on Q1 — see para 9?

~~4. Manufacturing industry responding to competitiveness gains [Commons Trade and Industry committee report 'The UK Motor Components Industry', published 16 July gives evidence that market share of imports of cars may drop below 40 per cent next year.] Report shows that depreciation of sterling in 1986 and recovery of domestic car output contribute to optimistic outlook for components industry. Export volumes (excluding oil and erratics) 6 per cent higher in second quarter than a year earlier.~~

5. Terms of trade (both including and excluding oil) in second quarter improved by 3 per cent over previous quarter.

Defensive

Current account deficit (of £2½ bn) forecast at time of Budget. Deficit only because exports, when UK growth running above long term trend and rest of world growth below long term trend. But May deficit shown to be freak:

1. Current account still in deficit. ~~But~~ deficit reduced by £359 million in June and deficit on manufactures reduced by £391 million. Current account in small surplus for year so far, which suggests overall deficit for 1987 below Budget forecast.

2. Strong domestic demand growth sucking in imports: ~~Not surprising that there should be some rise in imports given strong growth in domestic activity.~~ See above. Imports of intermediate goods and semi-manufactures rising as industry expands.

docs
pd - 6-8

3. Trend in imports upwards: Recent figures very erratic. Imports volumes (excluding oil and erratics) still below high level reached at end of last year. Too soon to say whether trend turning upwards.

4. Imports rising faster than exports [In second quarter on a year earlier, import volumes (excluding oil and erratics) up 9½ per cent, compared with 6 per cent rise for exports. On previous quarter import volumes up 5½ per cent while exports down 1½ per cent.] Not surprising given that UK economy is growing faster than most other major economies but exports likely to benefit from further improvements in world demand and UK's good competitive position.

5. Capacity constraint threatens current account performance. [Phillips and Drew forecast 2 July 1987 stated export boom unlikely to last as competitiveness declines and imports likely to increase since industry facing capacity constraint. Reported by Philip Stevens, Financial Times 6 July.] ~~Always expected imports to rise as economy grows strongly. FSBR forecast predicted 8 per cent rise in import volume (excluding oil and erratics) in 1987. Gains in competitiveness since end 1985 should help to restrain import growth and boost exports. Evidence of capacity constraints not conclusive. Industrialists report capacity utilisation relatively little changed over past year and still below 1973.~~ CBI in latest survey state "there is no evidence of widespread bottlenecks due to fixed capacity over the next twelve months", with capacity utilisation little changed over past year. Moreover significant part of import rise is intermediate goods and semi-manufactures for ~~exp~~ expanding industry.

6. Exports no longer growing. In second quarter, export volumes (excluding oil and erratics) 6 per cent higher than same period a year ago. Volume of manufactures exports 4½ per cent up over same period.

7. Industry Act forecast for growth in exports in 1987 too optimistic: Exports forecast to grow in 1987 as world trade rises and benefits of improved competitiveness continue to come through. Latest CBI survey show export orders still buoyant. Export volumes (excluding oil and erratics) 6 per cent higher in second quarter than a year ago.

Bit long. Perhaps better: "CBI survey says... Capacity utilisation little changed... ~~Some~~ Part of import rise is intermediate goods & semi-manufactures."

8. FSBR forecast of £2½ billion current account deficit in 1987 too optimistic: Current account of balance of payments shows small surplus in first half of this year.

9. Non-oil tradeable sector unable to respond owing to erosion of manufacturing base. [FT report on car components industry 30 June indicates many suppliers have disappeared although there is now some optimism following sterling's depreciation. Corroborated in Commons Trade and Industry select committee report on UK motor components industry]. Manufacturing industry doing very well - output up 4½% latest 3 months over a year earlier. CBI surveys consistently optimistic. ~~Performance of manufacturing industry improving. No reason for pessimism.~~ Volume of manufacturing exports (excluding erratics) ~~6~~ 4½ per cent higher in second quarter than a year earlier.

10. Fall in exchange rate needed - sterling's recent strength threatens competitiveness: Non-oil visible trade responding to 1986 exchange rate adjustment. Period of stability in exchange rate desirable (as endorsed by CBI). Vital that pay settlements kept under control if existing gains in competitiveness to be maintained.

11. UK's external position precarious: Current account in surplus in first half of 1987. FSBR forecast of current account deficit for 1987 only ½ per cent of GDP, following cumulative current account surplus of ~~some £19~~ almost £20 billion between 1979 and 1986. With net overseas assets thought to be worth around £110 billion by end 1986, overall external position in any case strong.

SECRET AND PERSONAL
UNTIL 11.30 am TUESDAY 11 AUGUST
THEN UNCLASSIFIED

TRADE FIGURES FOR MAY 1987

Advance circulation

Chancellor	Mr Peretz
Chief Secretary	Mr Kelly
Economic Secretary	Miss O'Mara
Sir P Middleton	Mr Culpin
Sir G Littler	Mr Barrell
Sir T Burns	Mr Owen
Mr Cassell	
Mr Sedgwick	Mr Norgrove - No.10

Circulation after 11.30 am on Wednesday 22 July

Financial Secretary
Paymaster General
Mr Monck
Mr Matthews
Mr Patterson
Mr Tyrie
Miss Roche - No.10

CONFIDENTIAL

Papers
PSR

NP

FROM: R FELLGETT
DATE: 11 August 1987

1. MR HAWTIN
2. CHIEF SECRETARY

cc Chancellor
Sir P Middleton
Mr F E R Butler
Mr Anson
Mr Hawtin
Mr Gilmore
Mr Turnbull
Mr Potter (o/r)
Mr S Kelly
Mr Cropper
Mr Tyrie

RECOVERING THE COSTS OF GRANT MAINTAINED SCHOOLS

Mr Ridley minuted the Prime Minister on 30 July. Mr Baker commented on 10 August.

2. In the immediate context of GM schools, the main point to note is that they are not attempting to re-open the question of financial neutrality. This is welcome. Nor does Mr Ridley argue again for a levy in place of grant abatement.

3. However, in the wider context of the reformed system of local government finance, Mr Ridley's approach has some potential dangers for us. All the emphasis is on producing a format for the community charge demand note, which shows that each local authority would need to raise the same community charge to support spending at GRE (£178 in 1987-88). This chimes with the DOE view that the important question in local authority finance is the level of rates and, in the future, community charge. Little emphasis is placed on local authority expenditure, and therefore little on GRE, even though it will become a norm for spending under the new system. DOE are prepared to manipulate GRE in

the way proposed to produce the "right" result for the community charge for spending at GRE, rather than accept the "wrong" notional community charge but more valid spending information. One odd consequence of this manipulation is that the GRE of a high spending LEA could be reduced to zero (or even become negative) if most of its schools opted for GM status.

4. In any case, the concept of a single community charge throughout the country to support spending at assessed need will be irrelevant during the transition. While there is a safety net in operation, the level of this notional community charge will vary considerably from area to area. If residents and voters are to obtain useful information from the community charge demand they need to be able to compare spending with the GRE norm, and with the previous year.

5. A comparison with the previous year is probably, in practice, more important; the holy grail of objective GREs accepted by everyone is unlikely to be achieved. It is therefore unfortunate that the skeleton demand notes illustrated in the annex to Mr Ridley's minute have omitted the comparisons with the previous year which were earlier proposed. If they had been included, it would in addition be clearer that spending and GRE appeared to fall by the same amount when a school opted out, whereas the authority was in fact spending 20% above GRE on each school.

6. The arguments for Mr Ridley's approach are stronger after the transition, although the dangers in focussing entirely on community charge rather than spending remain. But you have already commented that finance for GM schools will have to be reviewed if many opt out.

__Mr Baker's approach__

7. Mr Baker suggests instead that the spending of GM schools should appear in the demand note, as a separate item from the rest of LA spending. This item would then be entirely offset by the grant to GM schools. This approach avoids the manipulation of the GRE suggested by Mr Ridley; it produces sensible comparisons of actual spending with standard spending and a comparison of

the actual community charge with the same charge for spending at need that would appear on all demand notes. It has minor drawbacks: it makes the demand note a little more complicated and may leave some charge payers with the impression that GM schools are still run by local authorities. But on balance this approach looks more satisfactory than that suggested by Mr Ridley.

Conclusion

8. Mr Ridley does not seek to re-open financial neutrality or the decision on levy versus grant. But his approach to accountability is relevant only after complete transition to the community charge, and anyway raises some presumptions which are not in keeping with our concern for local authority expenditure (as part of general Government expenditure). I therefore recommend that you write to query the approach he is proposing, and to welcome Mr Baker's suggestion which appears to square the circle at the cost of a slightly more complicated demand note. A draft letter is attached.

9. HE agree.

N.I.Holgate

pp R FELLGETT

DRAFT LETTER FOR THE CHIEF SECRETARY'S SIGNATURE TO THE SECRETARY OF STATE FOR THE ENVIRONMENT

RECOVERING THE COSTS OF GRANT MAINTAINED SCHOOLS

Thank you for copying to me your minute of 30 July to the Prime Minister. I have also seen Kenneth Baker's letter of 10 August to you.

2. Your preferred approach to adapting the community charge demand note is designed to ensure that the charge for standard spending is the same (£178 in your example) in all local authority areas throughout the country. I understand why that should be your aim.

3. But residents should also be interested to see a clear comparison of actual spending with a defensible estimate of assessed need, and spending in any year with spending in the previous year. The examples in your annex omit the prior year's figures. (Had they been included, it would have been clearer that actual spending and assessed need changed by the same amount when a school opted for GM status, whereas in fact the authority in your example is spending some 20% higher than assessed need on its schools.)

4. Kenneth's suggestion is helpful. As he says, it makes clear

that residents will be financing grant maintained schools on the same basis as those maintained by local education authorities. I would be grateful if my officials could be involved in thinking through this option and in developing an arrangement for the existing rate support grant regime.

5. I am copying this letter to the Prime Minister, to other members of E(EP) and Sir Robert Armstrong.

[J.M]

CONFIDENTIAL

3

SECRETARY OF STATE FOR EDUCATION AND SCIENCE

ELIZABETH HOUSE
YORK ROAD
LONDON SE1 7PH
01-934 9000

12 August 1987

Wyn Roberts Esq MP
Minister of State
Welsh Office
Gwydyr House
Whitehall
London SW1A 2ER

Dear Wyn,

REFORM OF MAINTAINED FURTHER AND HIGHER EDUCATION: CONSULTATION PAPER

Thank you for sending me a copy of your minute to the Prime Minister of 7 August and the draft consultation paper on the reform of maintained further and higher education in Wales.

I am content with the further education aspects. However, I am concerned that paragraph 2.18 on corporate status will give the impression that the Government is having second thoughts about the policy behind our plans to remove the English polytechnics and colleges from local authority control. I appreciate that the paragraph is intended to relate only to Wales, but I can see our opponents seizing on it to suggest that we have changed our position since paragraph 4.7 of the Higher Education White Paper dismissed the GMP proposal for corporate status in the local authority context - or to suggest that we do not know what we are doing.

I therefore hope you can agree to delete the last two sentences of this paragraph and make one other change, to stress the Welsh context, as in the revised draft attached.

I am copying this letter to members of E(EP), to Tom King and to Sir Robert Armstrong.

Yours ever
Kenneth

KENNETH BAKER

2.18 The Government believes that, in addition to having the delegated powers outlined above, it would be appropriate for some colleges - in particular the large HE institutions in Wales - to have corporate status while still remaining within the local authority sector. Corporate status cannot guarantee greater independence for colleges from inappropriate controls. But in the right circumstances it can facilitate greater independence by enabling institutions directly to employ their staff, own their premises, enter into contracts, and generally to take greater responsibility for their own actions. The Government will therefore be considering ways to encourage the incorporation of colleges.

PWP

SECRETARY OF STATE FOR EMPLOYMENT

Caxton House Tothill Street London SW1H 9NF

Telephone Direct Line 01-213 6460

Switchboard 01-213 3000

David Norgrove Esq
Private Secretary
10 Downing Street
LONDON SW1

12 August 1987

Dear David,

RETAIL PRICE INDEX

... I enclose a copy of our note and draft press release on the Index of Retail Prices due to be released at 11.30 pm Friday 14 August.

Numbered copies also go to Alex Allan (Treasury), Sir Peter Middleton (Treasury), Timothy Walker (Trade and Industry), Rachel Passmore (CSO), John Footman (Bank of England), Chris Cloke (CO) and Sir Brian Hayes (Trade and Industry).

Yours sincerely,

Beverley Evans

BEVERLEY EVANS
Private Secretary

Reference 2

PERSONAL AND CONFIDENTIAL

MS EVANS

cc **PS/Secretary of State**
PS/Minister of State
PS/Secretary
Mr Manley
Mr Tucker
Mr P D Dworkin
Mr Sutlieff
Mr Sellwood
Mr Baxter

RETAIL PRICES INDEX

I attach a copy of the July RPI due for release on Friday 14 August 1987 together with a commentary and copies for the agreed circulation to No 10 and Departments (list filed inside).

Alex Craker.

STATISTICS D

D A CRAKER

12 August 1987

CODE 18-77

2

PERSONAL AND CONFIDENTIAL

GENERAL INDEX OF RETAIL PRICES : JULY 1987

The annual rate of inflation, as measured by the 12-month change in the retail prices index, rose to 4.4 per cent in July compared with the 4.2 per cent recorded for June.

2. The overall level of prices fell by 0.1 per cent in July, less than the decrease of 0.3 per cent recorded for the same period last year (when petrol prices fell by 3p a gallon on average). There were seasonal falls in the prices of many fresh foods and sale price reductions for clothing and footwear. Prices for motor vehicles and insurance were higher.

3. In August the 12-month rate is expected to remain at around 4½ per cent. There is likely to be an increase of around ¼ per cent in the overall level of prices between July and August, replacing in the 12-month calculation the similar increase of 0.3 per cent between the corresponding months last year.

Producer Prices

4. The annual change in the prices index for home sales of manufactured products was 3.6 per cent in July, much the same as in the previous four months. Over this period there has been a beneficial effect from the Budget in that this year there were no changes in duties on alcohol and tobacco replacing some increases from last year in the 12 month calculation. The annual rate of increase for the food drink and tobacco sector was 4.0 per cent in February and 2.0 per cent in July whereas the rate for the other sectores was 4.2 per cent in February and 4.6 per cent in July.

5. Prices for materials and fuels purchased by manufacturing industry were 8.3 per cent higher in July than a year ago. This was the fourth month in succession that these prices have increased above the previous year's levels, following a period of nearly two years when the 12 month change in prices was negative. Firmer petrol prices have been important in this changed position.

Tax and Prices Index

6. The tax and prices index increased by 2.8 per cent in the year to July compared with 2.5 per cent recorded for June.

PERSONAL AND CONFIDENTIAL

International comparisons

7. The latest 12-month percentage changes in consumer prices in the main OECD countries and the averages for all EEC and OECD countries are as follows:-

	UK	FRANCE	FEDERAL GERMANY	ITALY	NETHER-LANDS	JAPAN	USA	CANADA	OECD Averages	EEC Averages
1986										
Q1	4.9	3.6	0.7	7.6	1.2	1.6	3.1	4.2	3.8	4.4
Q2	2.8	2.4	-0.2	6.1	0.4	0.8	1.6	3.9	2.5	3.2
Q3	2.6	2.1	-0.4	5.4	-0.4	0.2	1.7	4.2	2.5	3.0
Q4	3.4	2.1	-1.1	4.4	-1.8	-0.5	1.3	4.3	2.1	2.9
1987										
Q1	3.9	3.2	-0.5	4.1	-1.2	-1.3	2.2	4.1	2.3	2.1
Q2	4.2	3.4	0.2	4.2	..	..	..	..	..	..
March	4.0	3.3	-0.2	4.2	-1.1	-0.8	3.0	4.2	3.0	3.0
April	4.2	3.5	0.1	4.2	-1.1	-0.2	3.8	4.5	3.5	3.1
May	4.1	3.4	0.2	4.2	-1.1	-0.3	3.8	4.6	3.4	3.1
June	4.2	3.3	0.2	4.4	..	..	..	..	..	..
July	4.4									

Note: With the exception of figures for the UK, all data for June, and for the second quarter of 1987 are provisional.

STATISTICS DIVISION
DEPARTMENT OF EMPLOYMENT 12 AUGUST 1987

153/87 August 14, 1987

GENERAL INDEX OF RETAIL PRICES

JULY 1987

The general index of retail prices for all items for July 14, 1987 was 101.8 (January 13, 1987 = 100). This represents a decrease of 0.1 per cent on June 1987 (101.9) and an increase of 4.4 per cent on July 1986 (384.7, January 1974 = 100).

The fall in the index between June and July was mainly the result of seasonal falls in the prices of many fresh foods and sale price reductions for clothing and footwear. Prices for motor vehicles and insurance were higher.

The movements for the main groups in the index are shown in Table 2.

Table 1.

	All items				All items except seasonal food		
	Index Jan 15 1974 = 100	Percentage change over 1 month	6 months	12 months	Index Jan 15 1974 = 100	Percentage change over 1 month	6 months
1987	Index Jan 13 1987=100				Index Jan 13 1987=100		
February	100.4	+0.4	+2.6	+3.9	100.3	+0.3	+2.5
March	100.6	+0.2	+2.3	+4.0	100.6	+0.3	+2.3
April	101.8	+1.2	+3.4	+4.2	101.6	+1.0	+3.0
May	101.9	+0.1	+2.6	+4.1	101.7	+0.1	+2.2
June	101.9	+0.0	+2.3	+4.2	101.8	+0.1	+2.1
July	101.8	-0.1	+1.8	+4.4	101.9	+0.1	+1.9

TABLE 2

	Indices (13 January 1987 = 100) June 9, 1987	July 14, 1987	Percentage change over the month
All items	101.9	101.8	-0.1
All items excluding food	101.9	102.1	+0.2
All items excluding housing	101.6	101.4	-0.2
Food	101.6	100.4	-1.2
Seasonal food	105.2	97.0	-7.8
Non seasonal food	100.9	101.0	+0.1
Catering	102.3	102.9	+0.6
Alcoholic drink	101.4	101.7	+0.3
Tobacco	99.8	99.7	-0.1
Housing	103.4	103.8	+0.4
Fuel and light	99.4	99.1	-0.3
Household goods	101.9	101.6	-0.3
Household Services	101.6	102.0	+0.4
Clothing and footwear	100.8	99.2	-1.6
Personal Goods and Services	101.9	101.9	0.0
Motoring Expenditure	103.2	104.4	+1.2
Fares and Other Travel Costs	101.5	102.2	+0.7
Leisure Goods	102.0	101.6	-0.4
Leisure Services	101.3	101.4	+0.1

NOTES TO EDITORS

1 The General Index of Retail Prices (RP1) measures the average change from month to month in the prices of goods and services purchased by most households in the United Kingdom. The expenditure pattern on which the index is based is revised each year using information from the Family Expenditure Survey. The expenditure of certain higher income households and pensioner households, mainly dependent on state pensions and benefits, is excluded.

2 The index is compiled using a large and representative selection of more than 600 separate goods and services for which price movements are regularly measured in about 180 towns throughout the country. Approximately 130,000 separate price quotations are used each month in compiling the index.

3 The prices of some items of food show significant seasonal variation. A separate price index is compiled for these "seasonal foods", the expenditure on which accounts for around 2½ per cent of household expenditure. The variation caused by these items is removed from the series of indices for 'all items except seasonal food'.

4 Rates of change of indices can be calculated over periods of any length. Rates calculated over long periods are slow to detect changes in trend while calculations over very short periods give rather volatile results. To help in assessing what is happening to prices, rates of changes in the all items index and the index for all items except seasonal food are shown in Table 1 over successive periods of one month, six months and twelve months.

5 Following the recommendations which the Retail Prices Index Advisory Committee made in its report submitted to the Secretary of State for Employment in July 1986, the index has been re-referenced to make January 1987 = 100. Calculations of movements in the index over periods of time which span January 1987 are made as follows:-

> The index for the later month (January 1987 = 100) is multiplied by the index for January 1987 (January 1974 = 100) and divided by the index for the earlier month (January 1974 = 100). 100 is subtracted to give the percentage change between the two months.
>
> Using the all items index for example: take the index for July 1987 (101.8) and multiply it by the January index (394.5) then divide by the July 1986 index (384.7). Subtract 100 from the result which gives 4.4 as the percentage change in the index over the twelve months to May.

6 The index for July 1987, if translated to the old reference date (January 1974 = 100) would be 401.6.

7 Other changes made to the index in 1987 are given in an article in the April edition of Employment Gazette.

8 The Retail Prices Index Advisory Committee was first established in 1946 and advises on the methodology used for compiling the RPI. Committee members include representatives of consumers, employees, employers, retailing organisations, academic experts, government departments and other official bodies. The Committee's latest report - 'Methodological Issues Affecting The Retail Prices Index' Cmnd 9848 HMSO £6.50 - was published on 15 July 1986. The Government announced at the same time that all its recommendations were to be accepted.

9 The housing costs of owner-occupiers are reflected in the index using an indicator which represents mortgage interest payments. A weighted average of building societies base mortgage interest rates is used in the calculation.

10 The index is given in full in the Employment Gazette.

PERSONAL AND C[...]ENTIAL

FROM: S PRICE
DATE: 13 AUGUST 1987

1. MR S J DAVIES
2. ECONOMIC SECRETARY

cc: PS/Chief Secretary
PS/Financial Secretary
PS/Paymaster General
PS/Economic Secretary
Sir Peter Middleton
Sir Terence Burns o/r
Mr F E R Butler
Mr F Cassell
Mr Kemp
Mr N Monck
Mr Odling-Smee
Mr Scholar
Mr Sedgwick o/r
Mr Bottrill o/r
Mr Davies
Mr Culpin
Mr Gilhooly
Mr Mowl
Miss O'Mara o/r
Mr Pickford
Mr Halligan
Mr Patterson
Mr Cropper
Mr Tyrie
Mr Call

THE JULY RPI (to be published at 11.30 am on Friday 14 August)

The level of the RPI fell from 101.9 to 101.8 between June and July. The twelve month rate of inflation rose to 4.4 per cent in July from 4.2 per cent in June. Excluding mortgage interest payments, the twelve months rate of inflation rose from 3.5 per cent in June to 3.7 per cent in July.

2. The fall in the index between June and July was mainly due to seasonal falls in the price of fresh foods and sale price reductions for clothing and footwear. Prices of motor vehicles and insurance were higher. The rise in the annual inflation rate between June and July reflects in part a 3p a gallon fall in petrol prices between June and July last year which has not been repeated this year.

3. In the City there is a narrow range of expectations of the change in prices between June and July, with James Capel, Goldman Sachs and Wood Mackenzie expecting no change, Phillips and Drew expecting -0.1 per cent, and Alexander Laing and Cruickshank expecting +0.1 per cent. The correct figure is -0.1 per cent.

Simon Price

S PRICE
EA1 DIVISION
x 5388

COVERING PERSONAL
AND CONFIDENTIAL

SECRETARY OF STATE FOR EMPLOYMENT

pmp

Caxton House Tothill Street London SW1H 9NF

Telephone Direct Line 01-213.......6460...............
Switchboard 01-213 3000

David Norgrove Esq
10 Downing Street
London
SW1A 2AA

12th August 1987

Dear David,

LABOUR MARKET STATISTICS

I enclose the revised pages for unit wage costs and productivity to be inserted in the draft press notice which was circulated on Monday. They remain personal and confidential until 11:30 on Thursday, 13 August.

I am copying this to Alex Allan (HM Treasury), Sir Peter Middleton (HM Treasury), Mr Hibbert (CSO), Mr Footman (Bank of England), Timothy Walker (DTI), Sir Brian Hayes (DTI) and Norman Blackwell (No 10 Policy Unit).

Yours sincerely

Peter Baldwinson

Peter Baldwinson
Private Secretary

COVERING PERSONAL AND

CONFIDENTIAL

SECRETARY OF STATE FOR EDUCATION AND SCIENCE

PRIME MINISTER

OPTING OUT OF ILEA: CONSULTATION DOCUMENT

I attach the draft of a consultation document on our proposals to allow inner London boroughs to opt out of ILEA. This follows closely the arrangements we have agreed in E(EP) and E(LF), but gives further details on a number of issues in particular the ground that will have to be covered in boroughs' applications to opt out. It has been seen in draft by officials in Departments with a close interest.

2. I should draw your attention particularly to two matters which we covered in earlier papers but on which the draft consultation document is silent -

(i) The draft says nothing about payments for detriment where ILEA central staff take up posts in the boroughs at a lower salary level, or about redundancy compensation for those staff remaining with ILEA who will be surplus to requirements as a consequence of opting out. These questions are closely associated with that of a manpower control for ILEA, which we are to discuss in E(EP) early in September. Unless we have reached a view before the consultation paper issues on the way in which such payments might be financed, there is little to be gained by raising the subject in consultation.

(ii) In our earlier consideration of the question of counter-obstruction I proposed that we might legislate to "fine" ILEA to the extent that it off-loaded surplus staff onto the opting out boroughs. John Major pointed out that there might be difficulties in applying such a "fine", and on reflection I have myself come to the conclusion that this is a sufficiently unlikely possibility for us not to need to provide against it in the Bill as introduced. It would be possible for us to reconsider this during the passage of the Bill if it appeared likely that ILEA were indeed unfairly loading the staffs of institutions in the opting out boroughs. It is not however a matter which the boroughs themselves see as a serious risk at present.

3. Paragraph 27 includes a passage in square brackets on community charge capping. I am very keen that we should say something on this, as it will be an important signal to the opting out boroughs and may indeed encourage some waverers to take the plunge. But what we say must clearly depend on where Nick Ridley has got to in formulating his proposals.

4. In order to allow a reasonable period for consultation, I must issue this document during the week beginning 7 September. I hope, therefore, that it will be possible to reach agreement on it in correspondence, although naturally if colleagues wish to discuss it early in September I shall be happy to do so. I should accordingly be very grateful if I could have any comments by not later than 4 September.

5. I am copying this minute to the other members of E(LF) and E(EP), to the Attorney General, and to Sir Robert Armstrong.

KB

KB 20 August 1987

Department of Education and Science

CONFIDENTIAL

DRAFT CONSULTATION PAPER

THE ORGANISATION OF EDUCATION IN INNER LONDON

Introduction

1. The Government wants the education service to become more responsive to the requirements of parents and employers. Some of the Government's principal educational initiatives bear directly on this objective - the delegation of financial responsibility to schools, more open enrolment, the establishment of grant-maintained schools and of City Technology Colleges are all particularly relevant. The influence of parents on the governing bodies of schools, and the powers of governors, are being enhanced by the Education (No 2) Act 1986. In higher education, the Government's proposal to re-establish the polytechnics and certain colleges as corporate bodies has as one of its main objectives the freeing of these institutions so that they can respond more rapidly to changing requirements.

2. The Government believes that in inner London special considerations apply which make it necessary to go still further towards ensuring responsiveness to local needs. The special circumstances of London have long been recognised. It has been argued that educational provision in the metropolitan area should be managed as a whole, with the resources to make available a wide range of provision to pupils and students who frequently travel across borough boundaries to receive education. But the logic of that argument leads in the direction of very large local education authorities (LEAs) which inevitably find it difficult to keep in touch with and match the requirements and aspirations of different areas. So far as outer London is concerned, this problem was resolved in 1965, when the outer London boroughs became the LEAs for their areas. They have now been carrying out education functions for nearly a quarter of a century.

It was argued that inner London's education had been planned and organised on a unitary basis since the 19th century and that individual inner London boroughs would be among the smallest LEAs in the country. Against this, there was severe criticism of the Inner London Education Authority (ILEA) on the grounds of its educational performance despite levels of expenditure far in excess of those of any other LEA in the country. The Local Government Act 1985 provided for the retention of a unitary authority. But the new ILEA has shown little sign that it is ready to tackle the root causes of its educational and financial problems.

4. The Government believes that the time has come to allow inner London boroughs the opportunity to demonstrate that they could provide an efficient education service within their areas. The forthcoming Education Bill will accordingly contain provisions designed to enable these boroughs to apply to become the LEAs for their areas. ILEA will continue to be the local education authority for the areas of those boroughs who do not choose to take advantage of this opportunity. The Government will of course continue to press ILEA to take the action necessary to improve its educational and financial performance.

5. This paper sets out the Government's proposals for the organisation of education in inner London. The comments of all interested parties are invited.

BROAD OUTLINE OF THE LEGISLATIVE PROPOSALS

Timing

6. Boroughs would be invited to apply to assume education functions from 1 April 1990. This will mean that transfer of responsibility would coincide with the proposed introduction of the community charge and the Unified Business Rate. By removing inner London's dependence on its present unevenly spread rate base, this will substantially remove the need for machinery to equalise London resources. The legislation would not allow boroughs which become LEAs to opt back into ILEA.

CONFIDENTIAL

Procedures For Opting Out

7. The legislation would provide that -

(i) Inner London boroughs and the City of London would be able to apply to the Secretary of State to assume the education functions in relation to their area subject to a resolution to that effect by the full Council passed by a simple majority. It would be open to one or more boroughs to make a joint application proposing a joint education authority or joint education committee for their combined area.

(ii) The applications should be submitted by not later than 28 February 1989 and should be published and made available to the public.

(iii) It would be open to any interested party, including other local authorities, to submit objections to the application. These objections should be submitted to the Secretary of State within a period of one month after the receipt of the borough's application, and should be copied to the borough concerned.

(iv) The Secretary of State should, after consideration of the applications and any objections, be able to make provision by means of a statutory Order subject to the affirmative resolution procedure of both Houses of Parliament for the transfer of the functions of local education authority for its area to a borough (or boroughs - see (i) above) or the City of London from the ILEA. Such transfers would have effect from 1 April 1990. The Orders would provide for the establishment within the authorities concerned of "shadow" LEAs for an interim period - probably from 1 September 1989 - in which they would be able to make the necessary preparations

(v) The Secretary of State would provide by statutory Order - subject to the negative resolution procedure of both Houses of Parliament - for the transfer from ILEA to the new LEAs of land, buildings and related assets and liabilities (see paragraphs 17-20 below).

(vi) ILEA would be placed under a duty to supply any information required by the Secretary of State or by the boroughs with respect to their application, to cooperate with the boroughs in the transitional period and to obtain the Secretary of State's consent before undertaking certain transactions.

(vii) Sections 18 and 19 and Schedule 9 of the Local Government Act 1985 would be amended so that the period of office of ILEA members for opted out boroughs would terminate on 31 March 1990, the Inner London Education Area would be redefined to exclude those boroughs, and the number of members of ILEA would be adjusted accordingly. Section 22 of the Act, which empowers the Secretary of State to review ILEA by 31 March 1991, would be repealed.

8. The timetable set out above is designed to lead to a transfer of responsibility for education in April 1990. It would however be open to inner London boroughs to apply to assume responsibilities for education from a later date.

Provision of Services

9. In considering an application from an inner London borough, the Secretary of State would require a detailed explanation of the way in which the borough would propose to fulfil its statutory duties if it became an LEA. The Secretary of State would need to be satisfied that the borough would be able to provide appropriate education for all its pupils and students,

including those with special educational needs, and that it would be able to provide inspectorial and other support services to meet its statutory duties and to maintain educational provision of a high standard. Boroughs would also need to show that they expect to make effective provision for the youth service, including appropriate support of voluntary organisations, and for a careers service. In some cases - perhaps particularly that of the careers service - authorities may wish to combine their own provision with co-operative arrangements with other LEAs. Where inner London boroughs would expect to inherit institutions of London-wide or regional significance, particularly in the case of further education or adult education, the Secretary of State would expect a commitment on the part of the borough to maintain such provision. He is mindful of the good record which LEAs - including small authorities - have in this respect.

10. As soon as possible after Royal Assent, guidance would be provided by Circular on the information which would be required from an inner London borough to support an application. This is likely to include -

- projected numbers of pupils and students, taking account of the flows of pupils and students in and out of the borough, set against the institutions available and their capacity;

- the property which the borough proposes to inherit for this purpose (see paragraph 18 below);

- policy on the organisation of nursery, primary, secondary and further education, including detailed proposals for the future of institutions offering provision of regional or national significance;

- policy on the school curriculum, including the borough's plans to secure effective arrangements for the progressive implementation of the national curriculum;

- the borough's approach to arrangements in hand in its schools and colleges under the education support grant, in-service training grant, and other specific grant schemes;

- policy on special educational needs, and the way in which the borough would propose to implement this - including arrangements for access to the services of educational psychologists - with projected numbers set against the institutional framework envisaged;

- the organisation proposed for the adult education service, the careers service, the youth service, the school health service, the education welfare service;

- the structure envisaged for the local inspectorate;

- the administrative organisation proposed;

- the recruitment procedure for the education department's central services;

- proposals for the establishment of an education committee in accordance with the provisions of schedule I to the Education Act 1944;

- information about the borough's overall financial situation.

11. Under existing legislation parents are entitled to seek places for their children in schools outside the LEA in which they reside, and students may similarly apply to colleges outside their area. These provisions will naturally apply in the case of any inner London borough which becomes an LEA. The arrangements for recoupment between LEAs will apply in London as elsewhere in respect of pupils and students attending schools and colleges outside their home LEA.

CONFIDENTIAL

The City of London

12. Like the other inner London authorities, the City of London would be eligible to apply to become the LEA for its area. The Secretary of State assumes that if the City chose to take advantage of this opportunity it would wish to make joint arrangements with another LEA; for example a neighbouring LEA might provide most services on its behalf. The Secretary of State will be prepared to enter into separate consultation with the City as necessary.

Staffing

13. The Orders referred to in paragraph 7(iv) above would provide for the block transfer to the new LEAs of the teaching staff linked to particular institutions in the boroughs concerned. This would mean that these staff would carry over their existing pay and conditions of employment. In the same way terms and conditions currently in force for lecturers in institutions of non-advanced further education would carry over to the new employers. Teachers not clearly linked to a particular institution, such as advisory and supply teachers or peripatetic teachers, would in general remain employed by ILEA, although it may be appropriate to provide for block transfer terms for those teachers the majority of whose work is at institutions in one of the new LEAs.

14. Certain categories of non-teaching staff, such as laboratory technicians and school secretaries, are clearly linked to particular institutions. It would be appropriate to provide block transfer terms for these staff. In other cases, such as school meals staff, it may be appropriate for the new LEAs to recruit directly to fill their staffing requirements. There may be further cases, for example some youth service workers, where it might be appropriate to provide for the transfer of groups of staff in designated services, as happened in some cases at the time of the abolition

15. It would not be appropriate to provide for block transfer terms for most of ILEA's central staff (administrators, inspectors and other groups of professionals such as educational psychologists). The boroughs would therefore for the most part recruit directly for these posts, enabling them to decide from the outset the size and structure of this part of their work force. The Government however believes that it would be right to require the boroughs, when making appointments within this category, to consider first applicants employed by ILEA. The boroughs would not be compelled to appoint such applicants in preference to those from elsewhere but this process should assist the reduction in ILEA's staffing which will be required as a consequence of a reduction in the scale of the authority's operation.

16. Under the Local Government Act 1985 the London and Metropolitan Government Staff Commission was set up to safeguard the interests of staff who would otherwise be made redundant by the abolition of the GLC and metropolitan counties. The Government's proposals to permit the transfer of education responsibilities will not lead to major staffing upheavals, but there will inevitably be issues arising which could best be dealt with by a similar Commission. The Commission might, for example, advise on the interfaces between block transfer, group transfer and individual recruitment by the opting out boroughs. Such a Commission would ensure that proper consideration was given to the interests of all the staff affected.

Transfer of Assets

17. The Government believes that the arrangements for transfer of land and buildings, together with the equipment located on or in them and associated rights or liabilities including related debt charges, should reflect where possible those that worked successfully in the case of the abolition of the GLC and the Metropolitan County Councils. The guiding principles for the transfer procedure should be continuity in the operation of educational establishments, clarity about where the title to

rights or obligations in respect of the property transferred.

18. The basic rule in identifying the property to be transferred would be that all the ILEA property within the boundary of the opting out borough should transfer when that borough became an LEA. In putting forward its application for this purpose the borough would have a duty to provide a complete list of the property which it believed it should inherit, making use as necessary of powers to be included within the legislation which would require ILEA to make available any necessary information. There would however be exceptions to this basic rule, as follows -

(i) Land or buildings which the new LEA did not propose to inherit would remain the property of ILEA.

(ii) The Secretary of State would determine the ownership of any institution falling within the boundary of an opting out borough, but which was the subject of a request by ILEA - within the period of one month allowed for objections to the application (see paragraph 7(iii) above) - that it should not transfer to the borough.

(iii) Where a borough could show that an ILEA establishment located outside inner London had provided regularly for a significant number of pupils or students resident in the borough, it would be open to it to argue that it should inherit that establishment in order to maintain a comprehensive service for its residents. This situation (like that described in (ii) above) could apply in the case of eg certain residential special schools. Determination of such cases would be a matter for the Secretary of State.

(iv) In the case of an institution mainly based in an opting out borough but having some of its facilities located outside that borough, including for example

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- The guidance to potential applicants (paragraph 10 above) would invite them to attempt to agree a solution with their neighbours in putting forward their application.

- In the absence of agreement, the Secretary of State would in general be guided by the principle that institutions should remain as an entity, and that they should transfer to the predominant owner, using the occupation of the largest area of floor space as an initial criterion, but taking account also as appropriate of the intensity of use (measured by pupil or student numbers). The latter criterion might be particularly appropriate in determining the ownership of playing fields. The Secretary of State would however have the power not to leave an institution with the predominant owner, if an overriding case had been made out by another authority for an exception to be made.

- It would be open to the loser in any dispute to negotiate user rights in property located within its own boundaries or to which institutions located in its boundaries had traditionally had access. The relevant property Order might require the owner to make available such rights.

19. Fittings, furniture and equipment in both educational institutions and other premises would transfer with the property in or on which they were located.

20. ILEA would be required to vacate the relevant premises by 31 March 1990.

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Education Assets Board

21. The forthcoming legislation will contain provisions establishing an Education Assets Board (EAB) to facilitate the transfer of assets in the context of the Government's proposals for polytechnics and colleges and for grant-maintained schools. The process of transferring educational responsibilities from ILEA will require decisions about property transfer which are no less complex than those arising in the other two cases. The remit of the EAB would accordingly include advising the Secretary of State on aspects of property transfer in the case of ILEA, and as necessary supervising the arrangements involved.

Protecting the Interests of Opting Out Boroughs

22. The Government wishes to ensure that inner London boroughs taking on education responsibilities should inherit without serious encumbrance the assets which they need for effective operation. The Secretary of State accordingly announced in the House of Commons on 22 July 1987 that the forthcoming legislation would require ILEA to obtain his consent in advance to the following actions:

- any disposal of land or interests in land, including buildings, used or held or obtained for or in connection with the authority's education functions;
- any contract for a consideration having a value in excess of £15,000.

The requirement in relation to contracts does not apply in the case of the inner London polytechnics, which are subject to a regime being applied in the case of all the polytechnics and colleges which are to be re-established as freestanding corporate bodies.

23. In discussion with ILEA the Department of Education and

Science has agreed arrangements for applying this regime which are designed to facilitate the effective day-to-day operations of the authority, while allowing the boroughs with a legitimate interest in particular transactions an opportunity to make their views known.

Other Government Policy Initiatives

24. The arrangements described in this paper will not affect the ability of schools' governing bodies to apply to the Secretary of State for grant-maintained status. Boroughs assuming education responsibilities in April 1990 will, like other LEAs, need to consider a scheme of financial delegation for the schools and further education institutions they will inherit. The Secretary of State will be prepared to receive representations from the boroughs on the questions of the timetable to which they should be required to work.

Financial Arrangements

25. From April 1990, a new system of local government finance will gradually be brought into operation. Instead of raising business rates specifically to finance spending in their own areas, every rating authority in England will levy a uniform business rate, the product of which will be distributed among authorities across the country according to their adult populations. In addition to a share of the national business rate, authorities will receive grant from the Exchequer so as to compensate for different levels of need and to contribute a fixed sum per person towards a standard level of service. The difference between this income and the expenditure of authorities in the area will be financed from the community charge together with domestic rates during the period 1990 to 1994.

26. Under this system, all inner London residents will benefit from central Government grant and a standard share of the national business rate in respect of education and other services. Local authorities in inner London will finance their total spending

after taking account of this income, from the community charge. ILEA will continue under these new arrrangements to issue a precept for budgeted spending to boroughs which remain within it. They will meet this precept from the sources of income described above, including the community charge.

[27. Under the new system, overspending on services will feed directly into the community charge. At ILEA's present levels of spending that would impose a considerable burden on community charge-payers in inner London. The Government is determined to use its power to limit rates and precepts to relieve the burden on inner London rate-payers over the next two years. It plans to phase in the charge over four years from 1990 so as to moderate the necessary changes in local spending and taxation. The Government is considering whether the new system should also include powers to limit rates, precepts and community charges to curb excessive local authority spending. It believes however that it would be unfair to impose such arrangements on boroughs which opt out of ILEA and which are not overspenders on other services. It therefore proposes that in the early stages of the transition an inner London boroughs which is not spending excessively on services other than education would not be designated under any selective scheme.]

28. If a borough is able to offer education more efficiently and effectively than does the remaining ILEA, it can pass the whole saving direct to its community charge payers. The Secretary of State is aware that several boroughs have announced their determination to provide a high quality education service at a realistic level of expenditure. He believes that the Government's proposals open the prospect of progress towards that objective.

Consultation

29. Comments are invited on the proposals set out in this document. They should be sent by 16 October to -

Mr P Cohen
Department of Education and Science
Room 3/54

20c/5

MR A. ALLAN
Room 14/2

FROM: MRS M HENSON
DATE: 20 AUGUST 1987

CHANCELLOR'S OFFICE	12/2
CST OFFICE	36/2
FST OFFICE	43A/2
EST OFFICE	52/2
SIR P MIDDLETON	78A/2
MR SCHOLAR	90/1
MISS O'MARA	97/2
MR P SEDGWICK	83/G
MR CULPIN	93/2
MISS SINCLAIR	89/1
MR B NAISBITT	43/3
Mr A HUDSON	13/2
MS C EVANS	93/1
MR PATTERSON	98/2
MISS SIMPSON	99/2
MR PICKFORD	95/2
MR J CARR	112/G
MR B S KALEN	98/3
MR HUNT	42/3
MR P BROOKS	110/G
MR KERLEY	98/2
MR BROOKS	41/3
MR BUCKLEY	90/2
MS HATTER	112/2
MR CROPPER	17/2
MR TYRIE	15A/2
THE DUTY CLERK	10 DOWNING STREET
MR S SHERBOURNE	10 DOWNING STREET
MR J R CALDER	I/R SOMERSET HOUSE
MR D H ROBINSON	DEPT OF FINANCE AND PERSONNEL ECONOMICS DIVISION RM 249A STORMONT BELFAST 3S15
MR P MAKEHAM	DTI Rm 601c 1-19 VICTORIA STREET LONDON SW1
MR GROOMBRIDGE	RM 536A, DHSS, NEW COURT, CAREY STREET, LONDON

AMENDMENT TO RELEASE DATES FOR ECONOMIC STATISTICS IN AUGUST

Please note that the "CBI Monthly Trends Enquiry (Aug)" is going to be published on Tuesday 1 September at 00.30 and not on Friday 28 August 13.00 as previously indicated.

Meena Henson
MEENA HENSON

Ch / To note esp X. PMP

11/8

GRS 122

Restricted

RESTRICTED
FM KINGSTON
TO ROUTINE FCO
TELNO 319
OF 101515Z AUGUST 87
INFO ROUTINE UKDEL IMF/IBRD WASHINGTON, UKREP BRUSSELS

YOUR TELNO 262

PRIME MINISTER'S VISIT : DEBT

TEXT OF PRIME MINISTERS LETTER HANDED TO BRICE, PRIME MINISTER'S DEPT ON 7 AUGUST.

2. BRICE THOUGHT THAT SEAGA WOULD BE GLAD TO HAVE THIS CONSIDERED COMMENT ON HIS IDEAS FOR DEALING WITH DEVELOPING COUNTRY INDEBTEDNESS. IT WAS ALREADY CLEAR THAT THE MARCH PAPER CIRCULATED BY SEAGA NEEDED MODIFICATION. BRICE WAS SURE THAT SEAGA WOULD WISH TO HAVE A TALK WITH THE CHANCELLOR OF THE EXCHEQUER IN BARBADOS IN SEPTEMBER, AND DESCRIBED THE PRIME MINISTER'S LETTER AS AN 'HONEST AND FRANK RESPONSE' TO THE DISCUSSION ON THIS SUBJECT DURING HER VISIT TO KINGSTON LAST MONTH.

X

PAYNE

YYYY

KGHPAN 3411

MONETARY DISTRIBUTION
WIAD

THIS TELEGRAM
WAS NOT
ADVANCED

Restricted

3461/022

FROM: MISS R STREATER

DATE: 21 August 1987

1. MR ~~BETENSON~~ MCB 21/VIII I agree.

2. MR ALLAN

cc PS/Chief Secretary
Mr Anson
Mr Hawtin
Mr Instone
Mr Ritchie
Mr Franklin

LORD SEEBOHM: HOUSING THE YOUNG HOMELESS

Mr Allen's minute of 3 August requested a draft reply for the Chancellor to send in answer to Lord Seebohm's speech in the House of Lords on 21 July in which he argued that housing the young homeless would have no effect on the PSBR or inflation.

2. I attach a draft reply which includes contributions from DOE, MP1 and PSF.

R Streater

MISS R STREATER

3461/023

DRAFT LETTER TO

Lord Seebohm

Thank you for your letter and the enclosed extract of your speech in the House of Lords on 21 July in which you [raised the issue of housing the young homeless.] argue that housing the young homeless would be self-financing.

[I am not sure exactly what you have in mind, but if the Government, or a public corporation, nurses, or participates in nursing, a loan from the general public in order to finance additional capital expenditure, then the PSBR will be increased to the extent of the increase in public sector liabilities. This will be the case regardless of whether the capital expenditure is undertaken by the public sector, or whether the finance is on-lent to the private sector for that purpose. We must control the PSBR because increases put pressure on demand and financial markets, other things being equal, stoking up inflationary pressures and raising interest rates.

Any offsets to a PSBR increase would feed through gradually from reductions in current spending - this would not help us cope with the immediate difficulties which a major increase in capital spending would create in managing the PSBR.]

? We believe that the best way to tackle homelessness is by encouraging the provision of private rented accommodation. We are committed to creating conditions in which landlords will have greater confidence to let property by striking a fairer balance between the interests of landlords and tenants. We will be bringing forward proposals to extend and develop the systems of assured tenancies and shorthold for new lettings to bring back into use many of the 550,000 private dwellings which remain empty as a result of present controls. Our proposals will also make the provision of new rented housing more attractive to investors.

Alongside this approach there are already a number of specific initiatives which address the problem of homelessness. Since April 1981, the Housing Corporation has approved schemes providing hostels and shared housing for over 15,000 people, about half for the single homeless. The Housing Corporation's 1987-88 programme includes £5 million for the 'Job Movers Scheme' which will provide housing for young, single people moving to areas of scarce accommodation to take up work. In addition, through our Estate Action initiative, we are helping bring council dwellings back to use to benefit the homeless; so far we have approved schemes for over 1100 dwellings, at a cost of over £5 million.

580/3

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FROM: COLIN MOWL
DATE: 21 August 1987

CHANCELLOR

cc Chief Secretary
Sir P Middleton
Sir T Burns
Mr F E R Butler
Mr Anson
Mr Byatt
Mr Cassell
Mr Sedgwick
Mr Hawtin
Mr Odling-Smee
Mr Spackman
Mr Turnbull
Mrs Lomax
Mr Potter
Mr Briscoe
Mr Ritchie
Mr Perfect
Mr Holgate
Miss Moore
Mr Cropper
Mr Tyrie

LOCAL AUTHORITIES' FINANCES: RECENT BEHAVIOUR AND PROSPECTS

Both before and during the June Economic Forecast we considered the past behaviour of, and prospects for, PCs' and LAs' finances in more detail than usual. The original stimulus for this work was the unexpectedly low PCBRs and LABRs in 1986-87. In the case of LAs this pattern appeared to be carrying through to 1987-88. The position at mid-June was that the LABR in the first two months was £¾ billion below the Budget profile. Prompted by this you asked us to take 'a hard look at what is happening to local authority borrowing and why' (Mrs Ryding's minute to me of 16 June, copy attached).

2. Mr Sedgwick sent you the results of our review of PCs' finances on 24 July (Public Corporations' Economic Performance and Finances: Recent Experience and Prospects). I now attach the results of our review of LAs' finances. The paper was written in PSF (mainly by Mr Briscoe and myself) in consultation with LG, with a substantial contribution from Mr Perfect in particular on creative accounting and capital spending. Its main findings are summarised in Section I.

3. The prospects section of the paper is based on the June Economic Forecast. Since that forecast was completed later information has perhaps made the LABR less a mystery than it was. At the time of the June forecast the picture for 1986-87 had become a little clearer than at Budget time as the paper points out. It was possible from the CSO's provisional national accounts data to explain, at least arithmetically, the fall in the LABR in terms of a higher LA current surplus and lower net capital spending, with the latter probably largely the result of creative accounting.

4. The June forecast revised the forecast of the LABR in 1987-88 down to £0.2 billion from £1.2 billion at the time of the Budget. This revision was largely the result of taking account of the borrowing outturns for the whole of 1986-87 (not available at the time of the Budget) and first two months of 1987-88. Only a small part of the revision could be justified in terms of changes to the underlying forecasts of LA income and expenditure. Since the June forecast was finished however we have had provisional LABR outturns for a further two months and a small upward revision to earlier months. The latest position, as reported in August's monthly note on the PSBR, is that the LABR in the first four months is zero, only £0.2 billion below the Budget profile, and much the same as in the first four months of last year.

5. My personal view - and annual leave has prevented a full discussion among the forecasters - is that in the June forecast we may have slightly overdone the downward revision to the LABR in 1987-88, but that this would not carry through to an upward revision to the PSBR as a whole because central government borrowing has been lower than expected. Even so the prospect would still be for an LABR not that much above the unusually low, but not unprecedented, 1986-87 level. We shall of course be reviewing the prospects again as part of the internal autumn forecasting exercise.

6. The other new information since the June Forecast comes from the RSG settlements for 1988-89 which were tougher than the forecast had assumed. Average rates increases close to double figures now seem probable.

7. Finally, aside from the problem of interpretation of the LABR with which this paper is concerned, you will recall that we reported in April a measurement problem (paragraph 4 of Mr Briscoe's minute of 22 April, copy attached for you only). The problem was a large discrepancy between the estimates for LA bank deposits derived from the banking returns on the one hand and from the LAs' own returns on the other. This raised doubts about the accuracy of the LABR figures although the statisticians' view was that the banks' figures used for the LABR were more likely to be correct. Thus far it has not been possible to explain or eliminate the discrepancy. Further action is planned and we will give you a full report when there is more concrete news.

X/

Colin Mowl

COLIN MOWL

LOCAL AUTHORITIES' FINANCES: PAST BEHAVIOUR AND PROSPECTS

This paper reviews the past behaviour of, and prospects for, local authorities' finances, concentrating on the local authority borrowing requirement (LABR). It considers in particular the large fall in the LABR in 1986-87 to unusually, but not unprecedentedly, low levels and whether this presages a sustained period of low local authority borrowing.

TABLE 1: LABR

£ billion

	1986 Budget Forecast	**1987 Budget Forecast**	**Latest Outturn/ Forecast**
1983-84	1.2	1.2	1.2
1984-85	2.4	2.4	2.4
1985-86	2.1	1.7	1.7
1986-87	1.6	0.5	0.3
1987-88		1.2	0.2
1988-89			0.4
1989-90			0.7

2. The paper is arranged as follows:

- Section I summarises the main conclusions.

- Section II provides an overview of local authorities finances over the past twenty years, paying particular attention to movements in the 1980s.

- Section III assesses the possible implications for the LABR of the "creative accounting" which local authorities have adopted in recent years.

- Section IV discusses the prospects for local authorities as seen in the June Forecast.

- Annex I describes how the LABR is measured and defined, and the availability of information on LA income and expenditure which might help explain movements in borrowing.

- Annex II summarises the individual creative accounting schemes whose implications are discussed in Section III.

I SUMMARY

3. The main conclusions of the paper are:

(a) Past Behaviour of LAs' Finances

(i) The **LABR** has on average been much lower in the 1980s than in the 1960s and the 1970s, less than half of one per cent of money GDP compared with earlier averages of over 2 per cent. Lower **capital expenditure and net lending** more than explain the lower level of borrowing in the 1980s. LAs' current surplus has been lower in the 1980s than in the earlier periods [paras 4-5].

(ii) The **share of the LABR** in total public sector borrowing has fallen. In the 1960s the LABR was on average larger than the PSBR, but fell to under half the PSBR in the 1970s and to well under one fifth in the 1980s [para 6].

(iii) About half of LAs' total **current receipts** comes from central government grant of various types and about one third from rates. The proportion of current expenditure financed by **grants** in total has been broadly flat in the 1980s, but the Aggregate Exchequer Grant percentage (of relevant expenditure) has fallen sharply. The latter helps to explain the faster real growth of net **rates** income in the 1980s than in the 1960s and 1970s [paras 8-10].

(iv) Although LAs' **current expenditure** has on average grown more slowly in real terms in the 1980s, its ratio to money GDP has increased slightly. Pay is the major element in current expenditure, accounting for nearly two-thirds of the total. **LA employment** expanded in the 1960s and early 1970s at 3-4 per cent per annum but contracted in the five years after 1976. Employment growth resumed in 1983-84 and has averaged 1½ per cent a year over the past four years. **LA average earnings** rose more slowly than those in the private sector in the 1970s and broadly in line with the private sector in the 1980s [paras 11-13].

This is a 79-81 phenomenon - ratio falling (slightly) since 87

(v) The lower level of **capital expenditure and net lending** in the 1980s is mainly due to lower gross domestic fixed capital formation (GDFCF). Lower net lending - mainly LA mortgages - also contributed but to a much smaller extent. Within GDFCF higher council house sales, a reduced rate of new housebuilding and lower acquisition of other capital assets contributed roughly equally [paras 14-15].

(vi) Sales of council houses and other existing assets count as negative GDFCF by LAs and positive GDFCF by the rest of the economy, with no effect on whole economy GDFCF. Excluding such transfers of existing assets the **volume of GDFCF** by LAs rose at an average 7 per cent a year in the 1960s but contracted at 4 per cent a year in the 1970s. It has continued to contract in the 1980s but at a slower rate. Moreover in the 1980s there have been contrasting trends in the components - new housebuilding has contracted at much the same rate as in the 1970s but other GDFCF has expanded [paras 16-19].

(vii) There was a sharp fall in the **LABR in 1986-87** to an unusually low, but not unprecedented, level; it was in surplus in 1981-82 and a slightly smaller deficit in 1982-83. Arithmetically the major part of the fall in borrowing was due to a higher current surplus, although recorded capital expenditure also fell significantly. The fall in capital expenditure was probably mainly due to increased creative accounting. There is no obvious explanation for the increased current surplus, but possibilities include recovery from lower than average surpluses in the two previous years, lower expenditure than expected when rates were set and high rating in the face of uncertainties about grant penalties [paras 20-21].

(b) Creative Accounting

(i) **Creative accounting** has reduced the LABR, mainly by allowing LAs to postpone full payment for some of the capital assets they are acquiring or already using. Deferred purchase, finance leasing and sale and leaseback all have this effect [paras 22-23].

(ii) Estimates of the effect of creative accounting on the LABR have been produced, both for the past and future, but they are highly uncertain. They suggest that creative accounting activity increased significantly in 1986-87, depressing the LABR and that the effect on the LABR in 1987-88 could be at least as large, if not a little larger [paras 24-27].

(c) Prospects

(i) The LABR forecast is subject to large **error margins**. The average absolute error on Budget forecasts of the LABR for the coming year is 0.4 per cent of money GDP, equivalent to £1.5 billion at 1986-87 levels of GDP. This compares with an average error on the PSBR as a whole of 1.1 per cent of money GDP, equivalent to £4.2 billion [para 29].

(ii) The **LABR** is forecast to be £¼ billion in 1987-88, the same as in 1986-87, and to be only slightly higher in 1988-89 and 1989-90, thus remaining well below levels experienced in the three years before 1986-87 [para 30].

(iii) **Current expenditure** is forecast to rise by 8-9 per cent in 1987-88, up from 7 per cent in 1986-87, and by 7½-8 per cent in 1988-89 and 1989-90. This implies overspends on relevant public expenditure, compared with the 1987 PEWP, of about £1 billion in 1987-88, £3 billion in 1988-89 and £5 billion in 1989-90 [para 31].

(iv) LA **average earnings** are forecast to rise by 8¾ per cent in the 1987-88 pay round, boosted by high figures for teachers and LA manuals, compared with 7½ per cent for private sector earnings. In subsequent pay rounds LA average earnings are forecast to rise broadly in line with the private sector plus a small premium for teachers ie. by 7½-8 per cent a year. LA **employment** is forecast to rise by 1 per cent a year, much the same rate as over the past two years [para 33].

(v) The forecast of expenditure implies that **Aggregate Exchequer Grant** will be 46 per cent of relevant expenditure in 1987-88, the same as the outturn for 1986-87. The forecast assumed that the outturn percentage would remain at this level from 1988-89 onwards but subsequent Government decisions on RSG imply a fall in 1988-89 to 45 per cent, on the basis of the forecast, not provision for, expenditure [para 34].

(vi) **Rates** poundage increased by about 7 per cent in 1987-88, and on the basis of the grant percentage <u>assumed</u> in the forecast, was forecast to rise by 7-8 per cent a year in 1988-89 and 1989-90. The subsequent RSG settlements were tougher than assumed, implying that rates could increase in 1988-89 by up to 3 percentage points more than in the forecast [para 35].

(v[illegible]) Net capital spending is forecast to be flat in real terms, but volumes of GDFCF (excluding council sales) are forecast to continue contracting [para 36].

II PAST BEHAVIOUR OF LOCAL AUTHORITIES' FINANCES

4. In analysing local authorities' finances the key distinction is between current account transactions - current spending, grant, etc - and capital spending. Table 2 gives an overall picture of LAs' finances using national accounts data.

TABLE 2: SUMMARY OF LAs' FINANCES

Current prices, £ billion, and % of money GDP

Annual Figures	Current Surplus		Capital Expenditure and net lending		Financial Transactions[1] and balancing item		LABR[2]		PSBR
	£b	%	£b	%	£b	%	£b	%	%
1963-64 to 1969-70		0.9		3.5		-0.1		2.5	2.3
1970-71 to 1979-80		1.1		3.3		-0.1		2.1	5.1
1980-81 to 1986-87		0.8		1.2		0.0		0.4	2.9
1980-81	1.9	0.8	4.0	1.7	0.0	0.0	2.1	0.9	5.4
1981-82	3.0	1.2	2.8	1.1	0.0	0.0	-0.2	-0.1	3.3
1982-83	2.7	1.0	3.2	1.1	-0.4	-0.1	0.1	0.0	3.1
1983-84	2.7	0.9	4.1	1.3	-0.2	-0.1	1.2	0.4	3.2
1984-85	2.1	0.6	4.0	1.2	0.5	0.1	2.4	0.7	3.1
1985-86	1.6	0.4	3.6	1.0	-0.3	-0.1	1.7	0.5	1.6
1986-87	2.6	0.7	3.0	0.8	-0.1	0.0	0.3	0.1	0.9

1 excluding net lending and financial transactions included in the LABR

2 LABR = capital expenditure and net lending plus financial transactions and balancing item less current surplus

Historic trends in the LABR

5. The most striking feature of table 2 is the much lower average LABR in the 1980s than in the 1960s and the 1970s, less than half of one per cent of money GDP, compared with earlier averages of over 2 per cent. The current surplus partly reflects the provision for repayment of debt that LAs are required to make. It has on average been close to 1 per cent of money GDP for most of the period since the mid-1960s, but it

was slightly lower in the 1980s than in the earlier periods. It is therefore the much lower level of capital spending in the 1980s that lies behind the lower borrowing rather than a higher current surplus. On average the residual in the accounts - the balancing item and financial transactions - was negligible in all three periods; but there can be large swings from one year to another. For example the reduction in the LABR in 1985-86 is more than accounted for by the change in the balancing item - the net change in measured income and expenditure pointed to an increase in borrowing.

6. Table 2 also contrasts movements in the LABR with those in the PSBR as a whole. The share of the LABR in the total has fallen from decade to decade. In the 1960s the LABR was on average larger than public sector borrowing in total. In the 1970s the LABR was just under half the PSBR and in the 1980s the share fell further to well under one fifth on average.

Current Receipts and Spending

7. Table 3 shows current spending and receipts as percentages of money GDP and annual growth rates in real terms. With the current surplus broadly constant, at around 1 per cent of GDP, total current receipts and total current expenditure have risen on average at broadly the same rate. This would be expected since authorities must keep their Rate Fund accounts - broadly analogous to the current account - in balance in the long run.

TABLE 3: LAs' CURRENT SPENDING AND RECEIPTS

real annual % increases and % of money GDP

	Total Current Expenditure: Real % inc	Total Current Expenditure: % of GDP	Total Current Receipts: Real % inc	Total Current Receipts: % of GDP	of which Total CG Grant: Real % inc	of which Total CG Grant: % of GDP	of which Net Rate Income: Real % inc	of which Net Rate Income: % of GDP
1963-64 to 1969-70	7	8¼	7	9¼	9	4¼	4	3½
1970-71 to 1979-80	4	10½	3	11½	5	6	2	3½
1980-81 to 1986-87	2	11	2	11¾	2	6	5	4
1980-81	2	11¼	4	12	4	6¼	7	3¾
1981-82	-1	11	2	12¼	-2	6	14	4¼
1982-83	0	11	-1	12	-3	5¾	4	4¼
1983-84	6	11¼	5	12	18	6½	-3	4
1984-85	2	11	0	11¾	-1	6¼	1	4
1985-86	-1	10¾	-3	11	-5	6	1	3¾
1986-87	4	10¾	6	11½	5	5¾	9	4

8. The two main components of current receipts, accounting for nearly 90 per cent of the total, are central government grant and rates. Total current grant as defined for the national accounts includes specific grant such as for the payment of housing benefit and mandatory student grants (as well as non-specific grant such as rate support grant. Table 4 shows for selected years total current grant as a percentage of current expenditure and, where available, the more familiar Aggregate Exchequer Grant (AEG) as a percentage of relevant expenditure. (In 1986-87 AEG was nearly £15 billion out of total current grant of over £22 billion).

TABLE 4: CURRENT GRANT AS PERCENTAGE OF EXPENDITURE

	1963-64	1970-71	1975-76	1979-80	1986-87
Total current grant % of current expenditure[1]	45¾	51¼	62½	53¼	54½
AEG % of relevant expenditure[2]	n.a.	n.a.	n.a.	59¼	46¼

1 UK cash basis; 2 GB accruals basis

9. The total grant percentage rose during the 1960s and early 1970s, peaking at over 62 per cent in 1975-76. It fell back during the rest of the 1970s but has been broadly flat in the 1980s. The total percentage does not give a true picture, however, of the impact of movements in central government grant on LAs' finances in the 1980s because it is affected by developments in grants for items of LA expenditure, such as housing benefit, which are almost wholly central government grant financed. The sharp fall in AEG as a percentage of relevant expenditure between 1979-80 and 1986-87 is a much better guide.

10. The growth of rate income reflects the buoyancy of the tax base due to new building, and modifications to existing buildings, as well as rate poundage increases. The squeeze on the AEG percentage in the 1980s is clearly reflected in movements in rate income (table 3). The growth of net rate income in real terms is higher, relative to both current expenditure and receipts, in the 1980s than in the 1960s and 1970s. Correspondingly the relative real growth of grant is lower.

11. LAs' current spending in real terms has grown at successively lower rates - with the 1980s so far averaging 2 per cent per annum compared with 4 per cent in the 1970s and 7 per cent in the 1960s - but the ratio

of current expenditure to money GDP has increased slightly. During the course of the 1980s the ratio has been broadly flat (table 3). The LAs' own paybill accounts for nearly two thirds of current expenditure. Table 5 considers the pay component in more detail.

TABLE 5: LA EMPLOYMENT AND EARNINGS

Annual % increases except column 1

	Employment			**Average Earnings**		**GDP Deflator**
	LAs*		**Private Sector**	**LAs**	**Private Sector**	
	level in millions	**%**	**%**	**%**	**%**	**%**
1963-64 to 1969-70	2.23	3.6				
1969-70 to 1979-80	2.70	1.6	-0.2	13.9	15.4	13.2
1979-80 to 1986-87	2.75	0.4	-0.6	10.1	9.8	7.6
1980-81	2.74	-1.6	-2.0	25.8	16.5	18.4
1981-82	2.70	-1.5	-3.9	12.1	11.5	9.9
1982-83	2.69	-0.4	-2.2	6.3	10.2	7.2
1983-84	2.74	1.9	-0.2	7.0	8.3	4.5
1984-85	2.76	0.9(0.5)	2.3	7.3	5.8	4.3
1985-86	2.79	1.1(0.6)	1.5	4.1	8.3	6.1
1986-87	2.85	2.2(1.8)	0.5	7.9	8.0	3.0

* headcount, full time equivalents where available are in brackets.

12. Local authority employment increased in each of the periods shown in table 5. It expanded at 3-4 per cent a year in the 1960s and early 1970s. In the mid-1970s however it slowed down sharply, with the level of LA employment peaking in 1976. Thereafter it fell at an average of 1½ per cent a year. Over the 1970s as a whole however LA employment increased. LA employment continued to fall in the early 1980s but has been rising since 1983-84, at an average of 1½ per cent a year.

13. LA average earnings rose more slowly than those in the private sector on average in the 1970s, and broadly in line with the private sector in the 1980s. LA average earnings have grown faster than the GDP deflator in both the 1970s and 1980s, particularly so in the latter period. This means that there would be real increases in LA expenditure on pay even if there was no change in numbers of employees. Alternatively numbers employed would have to fall to keep spending flat in real terms.

Capital Expenditure and Net Lending

14. Local authority **net capital spending** as defined for public expenditure control purposes comprises **gross domestic fixed capital formation**

(GDFCF) - eg. council house building net of council house sales, purchases of machinery and vehicles - <u>plus</u> net capital grants <u>plus</u> net lending by LAs. (In this paper net capital spending is sometimes referred to as "capital expenditure and net lending".) Table 6 shows changes in the composition of net capital spending, to which paragraph 5 mainly attributed the lower LABR in the 1980s, using national accounts rather than PES data.

TABLE 6: CAPITAL EXPENDITURE AND NET LENDING

% of money GDP

Annual Figures	**GDFCF**			**Net Capital Grants**	**Net Lending**	**Total**
	Land and existing buildings	**House building and repairs**	**Other**			
1965-66 to 1969-70	0.4	1.5	1.7	-0.2	0.1	3.5
1970-71 to 1979-80	0.3	1.3	1.6	-0.1	0.3	3.3
1980-81 to 1986-87	-0.5	0.7	0.9	0.1	0.0	1.2
1980-81	-0.2	0.9	1.0	0.0	0.1	1.7
1981-82	-0.6	0.7	0.9	0.0	0.2	1.1
1982-83	-0.7	0.7	0.9	0.1	0.1	1.1
1983-84	-0.6	0.8	0.9	0.3	-0.1	1.3
1984-85	-0.5	0.7	0.9	0.2	-0.1	1.2
1985-86	-0.4	0.6	0.9	0.0	-0.1	1.0
1986-87	-0.4	0.6	0.8	-0.1	-0.1	0.8

15. Table 6 shows that a reduction in GDFCF is the main reason for the lower level of net capital spending in the 1980s. Net lending, which mainly comprises LA mortgages, is also lower - and indeed is now negative with the value of new loans exceeded by that of repayments of old ones - but it contributes only a small part of the fall in net capital spending in total. GDFCF can usefully be divided into three components.

(i) Acquisition of land and existing buildings. In the 1980s this component has been dominated by council house sales. These count as negative investment (GDFCF) by LAs and positive investment by the personal sector. There is therefore no net effect on whole economy GDFCF.

(ii) New house building, and repairs to existing council houses.

(iii) Other GDFCF comprises purchases of plant, machinery and vehicles such as computers and dustcarts.

All three components of GDFCF have been lower in the 1980s than in the 1970s and 1960s, with the reduction much the same for each component.

16. Sales of council houses are simply a transfer of capital resources between different sectors of the economy, and do not represent a reduction in the total claims on the economy's resources. It is useful to look at GDFCF excluding sales of land and existing buildings. Even this measure is somewhat misleading however because in recent years LAs have been acquiring capital assets in ways which do not affect measured GDFCF, for example by finance leasing (leased assets are currently included in the owners' rather than the users' GDFCF). In this paper we look at GDFCF both including and excluding leased assets.

17. In the 1960s and early 1970s LAs' GDFCF (including leased assets but excluding sales of land and existing buildings) was a fairly constant proportion of whole economy GDFCF - around 17-18 per cent. But in the second half of the 1970s this proportion fell rapidly to about 10 per cent and it has remained at this level in the 1980s.

18. The implications of this picture for LA GDFCF in volume terms are summarised in table 7.

TABLE 7: VOLUMES* OF GDFCF (excluding acquisition of land and existing buildings)

	Annual % changes			
	Housebuilding and repairs	**Other**	**Total**	**Total plus leased assets**
1965-66 to 1969-70	6	8	7	7
1969-70 to 1979-80	-3	-5	-4	-4
1979-80 to 1986-87	-4	2	-1	0
1980-81	-25	-2	-14	-14
1981-82	-22	-10	-16	-13
1982-83	23	21	22	22
1983-84	8	3	5	6
1984-85	-5	5	1	2
1985-86	-4	5	1	1
1986-87	-3	-10	-7	-5

* cash figures deflated by movements in own (ie. GDFCF) prices

19. Several features of table 7 are worthy of comment:

- the reduction in council house building which began in the 1970s continued in the 1980s.

- Other GDFCF, on the other hand, has expanded in the 1980s following the squeeze in the 1970s.

- Leasing has made only a small difference to the overall picture in recent years.

The LABR in 1986-87

20. The LABR fell sharply 1986-87 to only £¼ billion. This was an unusually low level of borrowing but not unprecedented. The LABR was in surplus in 1981-82 and a slightly smaller deficit in 1982-83. Newly available national accounts data show arithmetically that the major part of the fall in borrowing last year was due to a higher current surplus, although recorded capital expenditure and net lending also fell significantly.

21. The fall in capital expenditure was probably largely due to an increased use of creative accounting by LAs. The main effect of this, discussed more fully in section III and annex II, was to allow LAs to postpone full payment for some of the capital assets they were using. There is no obvious explanation for the increase in the LAs' current surplus, which is not a concept easily related to the LAs' own accounting practices. The proximate cause was a large increase in rates relative to the increase in current expenditure (see table 5). Possible explanations include:

(i) The current surplus was smaller than average in the two previous years and the increase in surplus in 1986-87 was a return to more normal levels. The large rates rise in 1986-87 may therefore have been a deliberate attempt to compensate for perceived shortfalls in income in the two previous years.

(ii) Current expenditure may have turned out lower than expected when rates were set, because increases in teachers' pay were less than expected and because lower interest rates reduced interest payments.

(iii) LAs' may have rated high in the face of uncertainties about grant penalties.

III IMPLICATIONS OF CREATIVE ACCOUNTING

22. Creative accounting raises a number of policy issues, such as LAs' creditworthiness, the operation of public expenditure control mechanisms and value for money. This paper is concerned solely with the effect of creative accounting on the LABR.

23. Creative accounting has reduced the LABR, mainly by allowing LAs to postpone full payment for some of the capital assets they are acquiring or already using. Deferred purchase, finance leasing and sale and leaseback all have this effect (Annex II explains these schemes). In other words LAs can in the short term use the same amount of capital goods but with lower cash expenditure.

24. It is difficult, however, to quantify the effects of creative accounting. DOE have produced some tentative estimates, after consultation with LG and the Audit Commission. Table 8 summarises these estimates which must not be taken too literally. Not only are the estimates of total deals uncertain but so is the profile of spending for any given deal.

TABLE 8: EFFECT OF CREATIVE ACCOUNTING* ON THE LABR

£ million

	1984-85	1985-86	1986-87	1987-88	1988-89	1989-90
1. Cash spending on capital assets	300	200	200	100	300	500
2. Cash receipts from sale and leaseback	0	0	0	500	0	0
3. Acquisition of capital assets	200	500	1200	1000	300	100
4. Reduction in LABR (= 3-1+2)	-100	300	1000	1400	0	-400

* schemes covered here are deferred and advance purchase, finance leasing and sale and leaseback

25. The first row of table 8 shows the amount of cash expenditure on assets acquired through creative accounting arrangements, such as the rental payments on leased assets. The second row shows cash receipts generated from sale and leaseback deals. The third row shows the acquisition of capital assets through the various schemes. A large increase is shown in 1986-87 when the value of deferred purchase schemes and finance leasing rose sharply. The acquisition of these assets in 1986-87 at less than their full cost probably helped to reduce the LABR as shown in row 4.

26. Acquisition of assets via creative accounting is assumed to continue at broadly the 1986-87 level in 1987-88. While deferred purchase and leasing are now controlled, authorities can legitimately draw on facilities arranged before the controls were imposed. In contrast cash expenditure is fairly flat, and in 1986-87 and 1987-88 at levels well below values of the assets acquired. But it is the assumed high level of receipts from sale and leaseback in 1987-88 which gives a higher reduction in the LABR in that year.

27. Given the highly uncertain basis of these estimates, however, it would be dangerous to go much beyond the qualitative conclusion that creative accounting activity increased significantly in 1986-87, depressing the LABR, and that it could have much the same, or possibly larger, effect on the LABR in 1987-88 before easing back thereafter. By 1989-90 creative accounting could be increasing the LABR.

IV PROSPECTS

28. Table 9 summarises the June forecast of the local authorities' accounts. The forecast was completed before decisions on the RSG settlements for 1988-89, announced towards the end of July, were taken.

TABLE 9: LOCAL AUTHORITY TRANSACTIONS

	1985-86 Outturn	1986-87 Outturn	1987-88 Forecast	1988-89 Forecast	1989-90 Forecast
				£ billion	
Receipts					
Rates (net of rate rebates)	13.8	15.5	16.9	18.4	20.0
Aggregate Exchequer Grant	14.4	15.2	16.4	17.8	19.3
Other grants from central government	6.9	7.8	8.5	9.0	9.6
Other	5.9	5.9	6.7	6.7	6.8
Total receipts	40.9	44.4	48.6	51.8	55.6
Expenditure					
Current expenditure	38.4	41.0	44.5	47.9	51.7
Net lending and capital expenditure	4.3	3.7	4.3	4.4	4.6
Total expenditure	42.6	44.7	48.8	52.4	56.3
LABR (= expenditure less receipts)	1.7	0.3	0.2	0.4	0.7

29. Forecasts of the LABR are subject to large error margins. The average absolute error on Budget forecasts of the LABR made over the past ten years for the year just about to start is 0.4 per cent of money GDP. This compares with errors in the forecasts of the PSBR as a whole of 1.1 per cent of money GDP. At 1986-87 levels of money GDP the average absolute error on the LABR forecast is equivalent to £1.5 billion (the PSBR error is equivalent to £4.2 billion). The error in the 1986 Budget Forecast of the LABR was therefore in line with the past record.

30. The forecast of the LABR in 1987-88 has been revised down since the Budget by about £1 billion to a £0.2 billion, virtually the same level as in 1986-87. It is expected to be only slightly higher in 1988-89 and 1989-90 and is therefore not forecast to recover to the levels experienced in the three years before 1986-87.

Current Expenditure

31. Current expenditure is forecast to rise by 8-9 per cent in 1987-88, more than in 1986-87, when it rose by 7 per cent, and by 7½-8 per cent a year in 1988-89 and 1989-90. This implies the following overspends of relevant public expenditure compared with provision:

Overspends - £ billion

	1987-88	**1988-89**	**1989-90**
On 1987 PEWP	1.1	3.0	5.1
On provision in 1988-89 RSG settlement		1.9	n.a.

32. The forecast for 1987-88 is based largely on the LAs' budget statements. In the last four years the eventual spend has been about 1 per cent below that anticipated in budgets. However, for 1987-88 the forecast assumes that expenditure would turn out close to budgets, mainly because of the apparently low allowance for increased costs, particularly pay, in budgets. A second reason for assuming that expenditure will not fall below budgets is that the modifications to the grant system introduced for 1987-88 provide an incentive for authorities to show a cautious spending figure.

33. The forecast of current expenditure after 1987-88, which is not covered by LAs' budgets, is based on judgments about LA manpower, average earnings and the volume and price of procurement spending. Boosted by high settlements for the teachers and LA manuals, LA average earnings are forecast to increase by 8¾ per cent in the 1987-88 pay round, somewhat above the 7½ per cent forecast for the private sector. For the 1988-89 and 1989-90 pay rounds, LA earnings are assumed to increase in line with the underlying growth in private sector earnings, plus a small allowance for the residual effect of the teachers' settlement. LA manpower is forecast to rise by about 1 per cent a year (slightly less in terms of full-time equivalents), broadly in line with the recent past. The volume of procurement spending was assumed to rise by 1 per cent a year.

Current Receipts

34. The forecast outturn for **Aggregate Exchequer Grant** (GB accruals basis) in 1987-88 as a proportion of relevant expenditure is 46 per cent, much the same as in 1986-87. For 1988-89 and 1989-90 the forecast assumed that the outturn grant percentage would be broadly flat at the 1986-87 and 1987-88 levels. In fact subsequent decisions on the RSG settlements, announced on 23 July, imply a further fall in the grant percentage to 45 per cent in 1988-89, on the basis of the forecast of, not provision for, relevant expenditure.

35. The forecast made at the time of the Budget of an increase in **rates** income in 1987-88 of around 8½ per cent - consistent with a rate poundage increase of about 7 per cent - has been confirmed by later information. The forecast of current expenditure and assumption about Exchequer Grant pointed to rate poundage rising in 1988-89 and 1989-90 at a slightly higher rate than in 1987-88 ie. at 7-8 per cent a year. But both the expenditure provision and grant percentages in the RSG settlements were tougher than assumed in the forecast. This, together with the implied greater grant underclaim, suggests that the forecast rates increase in 1988-89 could be too low, by up to 3 percentage points.

Capital Expenditure and Net Lending

36. The forecast is for net capital spending to be broadly flat in real terms between 1987-88 and 1989-90. The volume of GDFCF (excluding council house sales) is forecast to fall however mainly because construction prices are forecast to rise more than prices generally as measured by the GDP deflator. The forecast implies modest overspending on net capital compared with the 1987 PEWP (see table 10). Although an overspend is shown for 1987-88 LG's latest view is that there is likely to be an underspend.

TABLE 10: NET CAPITAL OVERSPEND

£ billion

	1987-88	1988-89	1989-90
Overspend on 1987 PEWP	0.2	0.3	0.4

CONFIDENTIAL

ANNEX I: DEFINITION AND MEASUREMENT OF THE LABR

Definition

1. The LABR is the net amount of funds borrowed by local authorities (LAs) from other sectors of the economy. It is net in the sense that it is (gross) borrowing from central government, banks etc. net of any local authority lending to the central government and banks in the form of changes in LA holdings of government debt and bank deposits. It is also net in the sense that transactions between, and within, individual local authorities are netted out. Thus, although individual LAs make transfers between their different internal funds - and refer to these transfers as borrowing - such internal borrowing falls outside the scope of the LABR.

2. The LABR can be defined either in terms of the difference between expenditure and income which generates the need for finance or in terms of the transactions which provide the finance. This can be illustrated by the following simplified presentation of the LAs' accounts:

Generating LABR	1. Current income (mainly rates and grant)
	2. Current expenditure
	3. Capital expenditure
	4. Financial Surplus/Deficit (=1 2-3)
	5. Net lending
Financing LABR	6. Bank deposits and CG debt
	7. (Gross) borrowing

Measurement

3. In principle the LABR can be measured as well as defined in terms of either the income/expenditure side of the LA accounts or the financing side ie.

Either, from income expenditure: LABR = 2 + 3 + 5 - 1

or, from financing side: LABR = 7 - 6

In practice however there are errors and omissions in the accounts and the two methods give different answers. The difference between the estimates from the two sides of the accounts is known as the balancing item.

4. Partly because they are likely to be more accurate, but mainly because they are more timely, the financing figures are used to compile the published monthly estimates of the LABR. This is also the procedure for other components of the PSBR.

Revisions

5. The first estimates of the LABR are liable to revision. Revisions occur mainly when estimates based on information from all banks and local authorities replace estimates based on samples. The revisions are not usually greater than £50 million a month.

Income and Expenditure Data

6. Unlike for central government there is no monthly income and expenditure data for LAs which can be used to explain and interpret the borrowing figures. Although the CSO publishes quarterly data for the full income and expenditure accounts, with a lag of about three months, some of the key components for the current financial year are largely forecasts. For example some components of current expenditure are interpolations of annual forecasts based on LAs' budgets. There is quarterly data on capital expenditure however based on information provided for the capital control system.

7. The absence of comprehensive data on income and expenditure during the course of the year was a major problem in 1986-87 in interpreting the emerging LABR undershoot on the Budget profile, and drawing appropriate conclusions for the rest of the year.

ANNEX II: SUMMARY OF CREATIVE ACCOUNTING SCHEMES RELEVANT TO LABR

Deferred purchases

1. Around £1650 million of deferred purchase facilities were probably arranged in the year before July 1986 when deferred purchases of capital assets were brought under control. Local authorities remain free to use those facilities.

2. Under these deals the local authority acquires assets; typically over a period of two to three years with payments stretched over the following seven years. There is no effect on resources until the facility is used. At that point the local authority acquires assets without immediately affecting the PES or cash spending numbers. But when the payments fall due they will reduce the amount of new capital spending the authorities can undertake, unless provision is increased.

Advance purchases

3. Local authorities have also arranged advance purchase deals, in which they pay for goods before acquiring them. Some capital receipts were spent on such deals before annual spending power from capital receipts was reduced at the end of 1984-85. And the GLC arranged several such deals in 1985-86 before it was abolished, though the House of Lords ruled some were illegal.

4. In these deals the PES and cash spending effects are felt before assets are acquired.

Finance leasing (including forward leasing)

5. Local authorities were able to acquire assets by leasing them without using their spending power. This concession was removed as from 1 April 1987 but local authorities arranged forward leasing deals of around £1 billion, which can be used in future years.

6. The value of the asset scores in PES when it is acquired. But the cash expenditure is spread out over an extended period. So the growth in leasing will reduce cash spending associated with a given level of acquisition of capital assets and PES spending.

Sale and leaseback deals

7. These deals involve selling freeholds or leaseholds on assets and then leasing them back. The deals raise cash which can be used to generate interest payments that reduce net current spending, and so increase the level of Rate Support Grant the authorities receive. The cash can also be used to finance spending.

8. Earlier this year there were press reports that over £600 million of these deals were being discussed. However only £211 million of those deals are known to have been completed so far. These deals initially increase local authority receipts more than gross spending; so PES spending is reduced and cash flow improved. In the long run a higher level of PES and cash spending would be needed to maintain the use local authorities can make of resources.

ps2/32R

CONFIDENTIAL AND ~~PERSONAL~~

FROM: CATHY RYDING
DATE: 16 June 1987

MR MOWL

cc Sir T Burns
Mr Cassell
Mr Sedgwick

MONTHLY NOTE ON THE PSBR

The Chancellor was grateful for your minute of 15 June.

2. The Chancellor has noted in the summary of the note that the implications for 1987-88 as a whole are being reviewed in the economic forecasting round now under way. He would be grateful if you could ensure that this includes a hard look at what is happening to local authority borrowing and why.

CR

CATHY RYDING

3/16/6

3102/22

* Two things are worrying as 'embarrassments': The first is the message, in pages 9ff, that privatisation & wider share ownership did not take off until Mr M became FST in 1983 & that he was personally responsible for the take-off. This is wholly untrue: in particular, the propositions in Y are each & every one of them false. This rewriting of history is offensive not only to me, but will also offend others such as Sir G H [illegible] (as Mr M's predecessor) & Mr Tebbit (re BT). This is a major 'embarrassment' which must be corrected.

FROM: S J PICKFORD

DATE: 25 AUGUST 1987

MR D MOORE

cc Chancellor
Financial Secretary
Mr Culpin o/r
Mrs Lomax
Mrs Brown o/r
Mr Ilett
Mr Gunton

SPEECH BY JOHN MOORE

I attach a draft speech which John Moore intends to deliver on 5 September in the United States.

2. As you will see from the cover note, DHSS have sent the draft to us in order to ensure it contains no "embarrassments".

3. Since the speech covers Mr Moore's experiences as Financial Secretary with responsibility for privatisation policy, you may want to look carefully at those references. Mrs Lomax may also like to look at the figures quoted from the Treasury/Stock Exchange share ownership survey. DHSS have not given us any deadline for comments, but it would be prudent to send comments back as soon as possible. If you have comments we are quite happy to pass these back on the press office net. Alternatively, the Financial Secretary's private office could send them to Mr Moore's private office.

A minor 'embarrassment' is X, the suggestion that the opp[illegible] to council house sales came from within the Cons Party. It is [illegible].

Stephen Pickford

S J PICKFORD

GILL SAMUEL

We spoke about the attached draft of a speech which John Moore is due to deliver on 5 September in Indianapolis.

He is not seeking formal clearance but equally he does want to ensure that the draft does not contain any embarassments for DTI. The only potential embarassment I can see is on the British Telecom front - what do you think?

ROMOLA CHRISTOPHERSON

cc Nick Towers

5 .. share ownership
9 privatisation

INDIANAPOLIS SPEECH

FOURTH DRAFT

PHILOSOPHY INTO POLICY: HOW IT HAPPENS

I am particularly pleased and honoured to be here tonight on the eve of the Mont Pelerin Conference, because I feel I owe quite a large debt to the thinkers represented by the Society and it is satisfying to be able to say so publicly.

In April 1947 when the Society first met I was nine years old. Your historian, Mr. Hartwell, says the Society met because certain distinguished political thinkers saw the looming menance to personal freedom inherent in the post-war situation and were determined to fight against it. All through the next 25 years, as we know, their perception proved only too correct. For fully a quarter of a century the tide of illiberalism ran high and deep. Government power and its sinister control over the lives of individuals grew and grew. These were all my own most formative years and I remember with painful clarity the assumption throughout the political, academic and media worlds that ever greater Government intervention was a good thing and what was wanted was more of it, not less. The collectivists held the high ground, morally and intellectually, and anyone who questioned the prevailing wisdom was reviled and ridiculed.

In these dangerous times it was the men of the Mont Pelerin Society and their colleagues in, for instance, Britain's Institute of Economic Affairs, who kept alive an understanding of what constitutes a free society. I can still remember the excitement I felt on first finding and reading "The Road to Serfdom" and realising the philosophy of the free society was in fact alive and well - even if sadly disregarded.

Since I remember only too vividly the dominance and the arrogance of the collectivists throughout those years, I think it is not too much to say, as several before me have, that the flame of freedom might well have been snuffed out. It was kept burning by the kind of courageous people gathered at this conference - and that is why I feel such a debt of gratitude.

In 1974, when I first went into Parliament, despite the fact a socialist government was returned at that election, there were nevertheless, the first small indications that the tide of ideas might be beginning to turn. By 1979 it had turned enough to bring a Conservative Government to power, led by a radical champion of the free society.

The climate of opinion had undeniably changed; events had combined with intellectual argument to, in the words of Mao Tse-Tung, "change the water in which the fish swim" and so profoundly alter the lives of the swimmers. This was a transformation of immense significance, and its value will become even more apparent as the years go on.

So, when we came to power in 1979 we did so because prevailing attitudes had begun to turn against collectivism. This was very encouraging; and no one would underestimate its importance. But what had to happen then was that we working politicians had to somehow translate the ideas that had done so much to change attitudes into practical policies that actually worked to preserve, strengthen and extend the free society.

May I tell you, after 13 years in Parliament, 8 of them as a Minister, that this is harder than it looks.

What I would like to do tonight is tell you the story of just one such policy - one of a broad sweep of policies the Conservative Government has implemented to protect and increase personal liberty. It is a story, I think, that makes several points useful both to political thinkers and to those who try to implement their thoughts.

It starts with the belief that the two great bulwarks of a free society, the two institutions that are key to maintaining individual liberty, are the free market and private property, which is to say ownership.

On the first we have shelves full of brilliant writing, and a very great number of excellent speeches. Probably in large part because of this, we are winning the intellectual battle for the free market, which is a very great accomplishment indeed. But the fight for the idea of the free market has been so intense that it has tended to overshadow intellectual arguments for ownership, and on this key institution of the free society we have relatively little good modern writing.

Now I have often wondered why this should be so, and in thinking about it, it has occurred to me that most political thinkers, and indeed most politicians, come from backgrounds where people own things. Their families have houses, cars, property. It is to them part of the natural order of things, rather like air, and so unremarkable. They therefore tend to underestimate its power, both as a spur to individual action and as an essential foundation for individual freedom.

Here is where I have an advantage that some might call a disadvantage: my family did not own anything, until at last late in life they bought a tiny terraced house in the back streets of Brighton. So I know at first hand the fascination -- and the fear -- that ownership exerts on those who do not have it. I know at first hand the incentive that hope of ownership provides, and the lessons that the fact of ownership teaches. I know the feelings of responsibility that ownership creates, the sense of a personal interest in the stability and improvement of the community. I know that ownership teaches the finiteness of resources, the virtues of thrift and the risks and rewards of investment. I know, not in academic terms, but in very personal terms, that when you own something you feel independent, and when you do not you feel vulnerable.

Ownership diffuses power and prevents the concentration that is the prime ingredient of tyranny.

This is why I believe it so important that the spread of ownership be a key feature of our Government's long term programme to protect and extend the free society.

You will know, of course, of our spectacular success in increasing home ownership in Britain, achieved mainly by the sale of local authority houses to their tenants at a deep discount. This is a very good story in its own right, including especially the resistence we had to overcome within our own party. But what I want to tell you tonight is about a more sophisticated kind of increased ownership, and one which encountered even more bitter and determined resistence.

X

It is the story of how we have increased the ownership of equity shares from a point where barely 7 per cent of the population had any personal shareholding at all to now, where 20% - one in every five - of the adult population own equity shares themselves. And did it in less than four years, between 1983 and 1987.

To do this we had to start by overcoming the widespread ignorance in Britain of what shareholding actually is. One of the reasons for the ignorance was, sadly, because our education system was loathe to teach free enterprise capitalism. Many teachers did not understand it and some did not want to understand it. Incomprehension combined with distaste to create an impression, absorbed by many children, of something vaguely disreputable.

Another reason for the ignorance was because the few who did understand financial markets and operated them successfully, worked to cloak their activities in mystery. The phrase "Oh, he's something in the City," which has been used in Britain for years to describe virtually all financial employment, sums up the combination of confusion and prejudice with which even educated people viewed financial affairs.

Beyond the ignorance, we had to overcome the bitter ideological resistence of those people who think capital markets wicked by definition. We had to overcome the in-built resistence of the sophisticated people already dealing successfully in the equity markets, mainly with institutions, who thought it totally unnecessary to engage in the hard work of pursuing and servicing myriads of small investors.

We had to overcome the paternalistic view, widespread in my own political party, that ordinary people should not be allowed to risk their savings in the market, and last but hardly least, we had to overcome the plain snobbery that unfortunately still lurks in some dusty corners of British life.

On this last I must support my point by telling you that only a couple of years ago during a City lunch at which I was enthusiastically promoting the virtues of wider share ownership the Chairman of a major brokerage house actually said to me, "But surely we don't want all <u>those</u> kind of people owning shares, do we?"

It is always interesting to see how many people - intelligent, educated people - will pay lip service to an idea, for instance the idea of individual freedom; yet when it comes to implementing policies that will make the idea a reality - such as wider ownership - they resist them strenuously.

Why did we want to overcome all this? What is the point of extending equity ownership anyway?

Well, beyond the general virtues of ownership which I have just been extolling, it is because when we succeed in our aim of creating millions and millions of individual share owners, then for the first time great numbers of ordinary people will have flexible capital assets, and they will also have a supplementary source of income. This may not be large, indeed for most it will be very modest; but it will, for the first time, represent a new source of earnings and lessen the total reliance on a single wage packet which has meant a sometimes frightening dependency for many people. A flexible capital asset can open up opportunities and make possible an increased understanding never available before to ordinary people. There are some who will say this is too grandiose an interpretation of a modest share holding. But to someone who for the first time in his life has a tangible, even if limited, financial asset other than the fixed asset of a house, the implications are very large. He must face dilemmas - "Do I sell my shares now and put the money in the building society? Do I buy more shares? What is my present dividend? Is the company doing as well as it should? Could I do better with another company? Should I cash the shares in and put the money towards a new car?" Judgements of a whole new kind are required for the first time. Speaking as one who has gone though the process, I can say the potential for learning is enormous.

Wider share ownership is now seen as such a very good idea that it is difficult to even remember the massive indifference and in some cases overt hostility it inspired

The Government ministers concerned had to contend with an establishment view that

barely four years ago.

When I first went to the Treasury in 1983 my brief was tax and privatisation, and the official attitude was that the job was really tax ~~- privatisation was then very much out of favour after the Britoil and Amersham flotations which had been widely perceived as failures.~~ Establishment opinion then was that the privatisation programme was a bit of an embarrassment; ~~we might do a little more as our manifesto had pledged de-nationalisation and the Chancellor could use the money, but it was clearly indicated that whatever was done it should be done quietly with a minimum of fuss. Certainly no one was talking about~~ using privatisation as a vehicle for spreading share ownership.

I had proposed leaving all this out

and then

the Government had not yet convinced the sceptics of the scope for

Certainly

It was clear that we had to do two things immediately: first, we had to fight and win the intellectual battle for privatisation, which meant demonstrating beyond all doubt the failures of the nationalised industries, and the benefits to employees, to consumers and to the country of putting them into the free market. Second, we had to have a clearly defined long term strategy which would involve virtually every department of Government and thus focus the attention of the public and the politicians firmly on the programme.

We immediately embarked on both. I visited every Government Department and asked the same question: what in

I had proposed deleting these sentences and am inclined to press this

your Department is a fit target for privatisation and when can you do it? In many cases, I was greeted with a marked lack of enthusiasm. Officials saw privatisation as alot of work and trouble that would in the end reduce their own empires. Some Many politicians saw it as an unpopular and little understood scheme that would win no votes and might even lose some.

Nevertheless, by January 1984 the strategy for the next five years was complete, showing just what would be privatised and when each sale would take place. The strategy was then clearly endorsed by the Prime Minister and the Cabinet. But still, even then, a great many people, in and out of Government, did not think it would work. They certainly did not think it would work for British Telecom, which if privatised would be the largest equity sale the world had ever seen. The world's biggest previous equity sale had been a secondary offering of an already existing company - AT&T - which was only just over £650 million. BT was to be at least £xxxx. Conventional wisdom was convinced it couldn't be done - the financial markets simply would not be able to swallow such a massive offering.

It is interesting to note that it was here that necessity came to the aid of the believers in wider share ownership. It was clear to anyone contemplating the approaching BT sale that new markets would have to be tapped if it was to succeed.

Grudgingly it was accepted that if such a massive offering was to be successful it would have to attract a new audience, i.e. the mass public, as well as the traditional institutions. Even so, there was little confidence the mass public would buy it, and here is where the lack of understanding of the <u>passion</u> - it is not too strong a word - the <u>passion</u> for ownership that ordinary people have, showed most clearly. It was thought people would only buy the shares if they were bribed to do so, and the favoured bribe was to be vouchers which could be used to reduce the buyer's telephone bills.

Change "I" to "we"?

It seemed to me that while vouchers might very well work as a simple bribe (giving money away is usually popular), it did not focus on the objective of wider share ownership and completely ignored what I was certain was the dèsire for ownership among ordinary people. Instead of the vouchers, I supported the idea of the "small shareholders bonus," which would be a 10% dividend of extra shares for every small investor who kept his shares for over 3 years. This incentive had figured in the Britoil sale and had indeed attracted a remarkable number of small investors, but it had been completely overshadowed by the poor respose of institutions, who were influenced at the time by the drop in oil prices. Thus the suggestion of a small shareholders bonus for the BT sale was greeted with great disdain by the financiers - after all, they argued, if the

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lure of share ownership was not sufficient to induce purchase in the first place why would the prospect of more have any effect?

The battle over this was long and acrimonious. But as it was possible to demonstrate that the small share holders' bonus would be cost-free, it was finally reluctantly agreed to offer a choice of either the bonus or the telephone vouchers.

The financial sophisticates all said small subscribers would go for the vouchers. They were certain the cash-in-hand appeal of vouchers would prevail over the promise of shares in the future whose value was unknown. In the end, as you will know, the BT offering was heavily over subscribed, and it is one of the great satisfactions of my political life that 66% of all the people who subscribed opted for the small holders' bonus. Both the ability of ordinary people to understand the financial market, and their passion for ownership had been seriously underestimated. It has not been underestimated again. Every privatisation issue since has contained the promise of a bonus for small investors.

There is another part of the BT privatisation story which is important as a record of the battle for wider share ownership as opposed to simple de-nationalisation of a nationalised industry.

When the offering at last came to market it was, as I have said, wildly oversubscribed - quite beyond the expectations and even the hopes of those involved. The allocation meeting at which we were to determine which of the thousands and thousands of hopeful subscribers were to receive shares, not surprisingly, started in an exuberant mood. However, sharp differences soon surfaced. Many at the meeting insisted that the big subscribers should get all, or at least most, of what they asked for, and the little, often first-time investors - who after all might only have asked for the minimum number of shares (let's face it - not important investors) - should be left out. The preferred format was for what was called "proportionate scaling", which would mean the more shares applied for the more would be awarded Big subscribers would get a great many shares; small subscribers only a very few.

Had this happened I think it is fair to say that the brand new, still tentative, interest in share ownership by ordinary people, would have received a very serious blow. But it did not happen. After an exhaustive debate lasting several hours it was at last agreed - for the first time ever - to reverse tradition and stand proportionate scaling on its head. This meant the very smallest applicants - those who asked for only the minimum number of shares would get all they asked for, and as the applications got larger the proportion awarded would get smaller. Most radical of all, there was a cut-off point, above which no shares were allocated at all; so the very biggest subscribers got nothing.

Thus the small investor won on the crucial BT offering and has not looked back. Now after BT, British Gas, British Airways, British Airports Authority, and all the other offerings, fully 20% of the adult population in Britain are individual share-holders. There are, of course, many other strands to this success story, and it cannot be fairly told without mentioning the impact made by the removal of tax barriers and the improvement of the tax climate for small investors, which have acted as important incentives to equity share purchase.

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Now it seems to me there are several useful lessons to be learned in considering the wider ownership programme in Britain. First, of course, is to recognise that the passion for ownership does exist in almost everyone. It is no good saying, as the socialists do, that private property is wicked and public property is virtuous; it simply is not true.

It is also no good saying, as some Conservatives, even in the 1980s have been heard to say, that ordinary people are not up to coping with capital assets; that has been demonstrably proved false.

A second useful lesson is to see that the capitalist spirit - which is simply a willingness to invest and take risks in the hope of bettering one's condition - is a part of virtually <u>everyone's</u> make-up and only awaits opportunity to spark action. It would seem, therefore, an urgent task to get busy and create more opportunities.

There is a third lesson; one which comes from looking at the results of the wider ownership programme in terms of its effect on the individual human personality. In my constituency in Croydon we have many very large public housing estates - Council houses. In many of them, sadly, the look and mood is what we have come to expect of public housing - bleak, gray, vandalised, grim. But over the last eight years of Conservative government quite a few of them have been sold to their tenants at substantial discounts. I can only say to you the transformation is incredible. One can drive through the estates now and instantly identify the houses that are owned by their occupiers - new front doors, shutters, wonderfully pruned and planted gardens, flagstone paths, patios --- vivid testimony to the power of ownership to foster pride and inspire effort. And I can tell you as their constituency M.P. that it has a marked effect on their interest in Government measures that might affect their property. It is as if owning their home has enfranchised them in a way the simple fact of a vote never did.

So, in conclusion, I think it is possible to look at the privatisation programme in Britain, certainly to date, with a good deal of satisfaction. In the unending struggle to maintain and extend the free society we have first to win the battle of ideas, but then it is necessary to secure the gound won with practical political measures. Loooked at in this light the privatisation programme has reduced the role of he state, has re-invigorated the free market, and has spread ownership of a new kind more widely than ever before. One hopes that we can go on to design and implement many many more programmes and policies that do as much.

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3362/48

FINANCIAL SECRETARY TO THE TREASURY

FROM: N WILLIAMS
DATE: 28 August 1987

MR DAVIS EA2

PS/Chancellor
PS/Chief Secretary
PS/Economic Secretary
Sir P Middleton
Sir G Littler
Sir T Burns
Mr Cassell
Mr Sedgwick
Mr Peretz
Mr Bottrill
Mr Kelly
Miss O'Mara
Mr Culpin
Mr Borrell
Mr Owen
Mr Norgrove No 10

JULY TRADE FIGURES

1. This is to confirm that the Financial Secretary was content with the draft briefing for I.D.T attached to your minute of 27 August, subject to the amendments which I passed on to you by telephone this morning (which were incorporated in the revised briefing attached to your minute of 28 August).

N Williams

NIGEL WILLIAMS
(Assistant Private Secretary)

Covering Secret And Personal

From: Paul Davis
Date: 28 August 1987

PS/Financial Secretary

cc PS Chancellor
PS Chief Secretary
PS Economic Secretary
Sir P. Middleton
Sir G. Littler
Sir T. Burns
Mr Cassell
Mr Sedgwick
Mr Peretz
Mr Bottrill
Mr Kelly
Miss O'Mara
Mr Culpin
Mr Burrell
Mr Owen
Mr Norgrove No10

July Trade Figures.

1. I have incorporated the suggestions made by the Financial Secretary in the draft briefing for IDT, and I attach a revised version.

Paul Davis

EA2 35A/3 x5384

SECRET AND PERSONAL
UNTIL 11.30 am TUESDAY 1 SEPTEMBER
THEN UNCLASSIFIED

DRAFT BRIEFING FOR IDT

Positive

1. Export volumes (excluding oil and erratics) in three months to July 6 per cent higher than a year earlier - stronger growth than in most other developed countries.

2. CBI Survey for July shows export order books still buoyant.

3. Terms of trade (both including and excluding oil) in three months to July improved by 2½ per cent over previous quarter.

Defensive

1. Current account deteriorated by £170 million in July as a result imports growing faster than exports since June. Monthly figures erratic but deficit of £310 million in June leaves only modest current account deficit of £369 million so far in 1987. Deficit only to be expected when UK growth running above long-term trend and rest of world growth below trend.

2. Current deficit widening. Current deficit of £369 million for year so far lower than £1848 million deficit in second half of 1986. Out-turn so far this year better than £2½ billion deficit expected at Budget time.

3. Current account deficit in 1986 worse than thought previously. Pink Book estimate of 1986 current account deficit £980 million, up £860 million from previous estimate. Current account balance of large flows, hence small revisions can cause large changes in balance.

4. Strong domestic demand growth sucking in imports: Intermediate goods and semi-manufactures continue to make a large contribution to rise in imports, reflecting expansion of UK industrial output.

5. <u>Trend in imports upwards</u>: Recent figures very erratic. Imports volumes (excluding oil and erratics) so far this year still below level in second half of last year.

6. <u>Imports rising faster than exports</u> [In three months to July on a year earlier, import volumes (excluding oil and erratics) up 10 per cent, compared with 6 per cent rise for exports. On previous three months import volumes up 8 per cent while exports down $1\frac{1}{2}$ per cent.] Not surprising given that UK economy is growing faster than most other major economies. Gains in competitiveness since end 1985 should help to restrain import growth and boost exports.

7. <u>Capacity constraint threatens current account performance</u>. [Phillips and Drew forecast 2 July 1987 stated export boom unlikely to last as competitiveness declines and imports likely to increase since industry facing capacity constraint. Reported by Philip Stevens, Financial Times 6 July.] Always expected imports to rise as economy grows strongly. Industrialists report capacity utilisation relatively little changed over past year. CBI in latest survey state "there is no evidence of widespread bottlenecks due to fixed capacity over the next twelve months".

8. <u>Exports no longer growing</u>. In three months to July export volumes (excluding oil and erratics) 6 per cent higher than same period a year ago. Volume of manufactures exports $4\frac{1}{2}$ per cent up over same period.

9. <u>FSBR forecast for growth in exports in 1987 too optimistic</u>: Exports forecast to grow in 1987 as world trade rises and benefits of improved competitiveness continue to come through. Latest CBI survey show export orders still buoyant. Export volumes (excluding oil and erratics) 6 per cent higher in three months to July than a year ago.

10. <u>FSBR forecast of £$2\frac{1}{2}$ billion current account deficit in 1987 too optimistic</u>: Out-turn so far this year better than expected. Current account of balance of payments shows only small deficit in year so far.

11. Non-oil tradeable sector unable to respond owing to erosion of manufacturing base. [FT report on car components industry 30 June indicates many suppliers have disappeared although there is now some optimism following sterling's depreciation. Optimistic outlook corroborated in Commons Trade and Industry select committee report on UK motor components industry]. Manufacturing industry doing very well - output up 4½ per cent comparing latest three months with a year earlier. CBI surveys consistently optimistic. Volume of manufacturing exports (excluding erratics) 4½ per cent higher in three months to July than a year earlier.

12. Fall in exchange rate needed - sterling's recent strength threatens competitiveness: Non-oil visible trade responding to 1986 exchange rate adjustment. Period of stability in exchange rate desirable. Vital that pay settlements kept under control if existing gains in competitiveness to be maintained. Endorsed by CBI.

13. Invisibles revised down in 1987 Q1 - implications for Q2? Revision to 1987 Q1 invisibles figures made in light of Pink Book and other new information. Estimates for 1987 Q2 to be published on 17 September.

14. Invisibles revisions delayed: New procedure should contribute to improved quality of quarterly invisibles estimates and reduce the need at least for short-term revisions.

15. UK's external position precarious: Current deficit modest so far in 1987. FSBR forecast of current account deficit for 1987 only ½ per cent of GDP, following cumulative current account surplus of almost £20 billion between 1979 and 1986. With net overseas assets worth around £114 billion by end 1986, overall external position in any case strong.

3462/017

CONFIDENTIAL

FROM: M C BETENSON

DATE: 28 August 1987

CHIEF SECRETARY — spoke to Jill. They have this thought on board already. CE.

Re the draft papers, I am content that the ~~[illegible]~~ matters [illegible] to continue. Concerned that the evaluation will ~~[illegible]~~ take 3 yrs to evaluate a pilot HAT. JB

cc Chancellor
Financial Secretary
Economic Secretary
Sir Peter Middleton
Mr F E R Butler
Mr Anson
Mr Burgner
Mr Hawtin o/r
Miss Peirson
Mr Turnbull
Mr Instone o/r
Mr Gibson
Mr Nicol
Mr Cropper
Mr Call
Mr Tyrie

HOUSING POLICY AND HOUSING ACTION TRUSTS

Mr Ridley is proposing to circulate further housing policy papers for an E(LF) meeting on 8 September. We have yet to see a paper which will cover a revised draft White Paper, and I will provide advice on that once it is available. However, DOE are seeking urgent clearance of the two attached draft papers: a report on general progress and outstanding issues; and a further detailed paper on Housing Action Trusts (HATs).

BETENSON TO CST 28/8

Issues

2. The progress report notes: that most remaining issues are being taken forward in correspondence; that proposals for ring-fencing local authority housing accounts are being revised for later collective discussion; but that differences remain between Treasury and DOE on the scale and rate of progress of a HATs programme, which require decision.

3. The detailed paper on HATs sets a framework for selection of HAT areas and evaluation of performance; it also costs an example of a possible HAT in Leeds. E(LF) (13th meeting) asked Mr Ridley to bring forward a paper agreed with you. We have discussed the

paper with DOE in draft and they have accepted a number of amendments. I think the result represents acceptable progress, although we need to pursue with DOE at official level how exactly selection criteria and performance targets will be quantified. The detailed costings of a programme will depend on which areas are selected for HATs, but, on the basis of the Leeds example, Mr Ridley's PES bid would provide scope for at least 15 HAT designations over the Survey period. The Leeds costings appear reasonably based and include allowance for housing benefit implications. DHSS will however need to agree the housing benefit calculations. The framework for selection and evaluation will allow performance targets and minimum criteria for selection and assessment of success to be developed as individual areas are considered in detail as HAT candidates.

4. We would be content to take this work and associated costings forward with DOE on a bilateral basis. Survey decisions will provide a cap on the number of designations which DOE can make and any individual designation will need to be assessed in terms of cost and value for money against the constraint of Survey resources. Treasury approval will be required for any individual designation.

5. However, both the HATs paper and the progress report make clear that Mr Ridley wishes to proceed with between 15 and 30 HAT designations over the Survey period (depending on the cost of individual HAT nominations), consistent with his Survey bid. This would be much more than the pilot approach which E(LF) agreed in principle at its 13th meeting; and the rolling programme envisaged by Mr Ridley would allow HAT designations to continue before evaluation of the initial HATs is complete, so that it would be difficult to slow the momentum of the programme if the evaluation is adverse or suggests a change of direction.

6. In order to ensure value for money, and to prevent an initiative from proceeding at half cock, there are grounds for pressing for evaluation of a pilot scheme before a decision is taken to move on to a rolling programme. And unless E(LF) restricts HATs initially to a pilot scheme, the pressure on you to concede much of Mr Ridley's Survey bid of £20m, £100m and £150m would be intensified. It might

be difficult to hold to the Survey fallback we are proposing of £20m, £50m and £70m. Both the progress report and the detailed HATs paper mention Treasury concerns.

Recommendation

7. I recommend you agree the DOE paper as a basis for further work on the HATs initiative. You can also accept what the progress report has to say on general issues. However, although the progress report and the detailed HATs paper mention Treasury opposition to a substantial rolling programme of HATs, it would be worth expanding on our concerns in a Treasury paragraph.

8. I attach a possible draft paragraph for you to consider. I have also suggested some manuscript amendments to the progress report as it stands. Since the Leeds HAT costings are only an example, and DOE accept that they do not allow firm conclusions to be drawn for a programme as a whole, the draft draws attention to the dangers of proceeding with a full scale programme on that basis.

9. Any amendments to the DOE draft will need to be made quickly given the need to circulate papers well in advance of E(LF).

Martin Betenson

M C BETENSON

CONFIDENTIAL

DRAFT TREASURY PARAGRAPHS

The Treasury accepts that the paper on Housing Action Trusts provides a basis for further work on the selection of HAT areas and the evaluation of performance. But the Treasury believes that any programme of initial HAT designations should be restricted to a pilot basis, with perhaps 2 or 3 HATs being set up in the next 3 years.

A larger programme of HAT designations would mean that the HATs policy could not be properly evaluated in advance of a substantial commitment of public funds. We would risk committing significant public expenditure without a firm assessment of whether it represented value for money or whether the policy was targetted in the most effective way. A HATs pilot of 2 or 3 schemes could be evaluated over the next three years and an expansion could be agreed before the end of this Parliament if the approach proved successful. This would ensure that public money is effectively targetted and would not diminish the resources available for wider initiatives which colleagues may wish to pursue.

The only costings of an HATs' initiative which we have at present are based on the Leeds example. The Department of the Environment accept that the costings cannot form the basis for an assessment of a wider programme of HAT designations because of the potential for cost variations from area to area. It would therefore be wrong to establish now a rolling programme of designations which could later prove to have too specific a cost base. We should instead move forward cautiously, making firmer general estimates of costs and basing any expansion of a HATs' programme on a comprehensive assessment of the approach and the outputs achieved by the initial limited pilot programme we originally agreed.