PO-CH/NL/0232

PART C

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PART C

SECRET

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PART C

CHANCELLOR'S PAPERS ON PUBLIC EXPENDITURE PROGRAMMES AND THE PUBLIC SECTOR BORROWING REQUIREMENT (PSBR)

PO -CH /NL/0232
PART C

Begins: 18/1/88
Ends: 24/2/88 (CONTINUED)

DD: 25 years

20/9/95

COVERING CONFIDENTIAL AND PERSONAL

From: COLIN MOWL
18 January 1988

CHANCELLOR

Copy with PPS letter, attached, for:

Mr Gray - No. 10

cc List A

Economic Secretary
Sir P Middleton
Sir T Burns
Mr Scholar
Mr Sedgwick
Mr Peretz
Mr Watts
Mrs Todd
Mr Ritchie
Miss Chapman

List B (distributed at 11.30am, 19 January)

Chief Secretary
Financial Secretary
Paymaster General
Mr J Anson
Mr Moore
Mr Odling-Smee
Mr Culpin
Mr Turnbull
Mrs Brown
Mr Bottrill
Mrs Butler
Mr R I G Allen
Mr Grice
Miss O'Mara
Mr Richardson
Mr A Hudson
Mr Franklin
Mrs Ryding
Mr Cropper
Mr Tyrie
Mr Call
Mr Calder - IR
Mr Allen - C and E

MONTHLY NOTE ON THE PSBR

I attach a report on the PSBR outturn for December, and a comparison with the forecast made a month ago. The December outturn will be published by press notice at 11.30am on Tuesday 19 January.

In line with the practice followed at this time last year, the note does not contain a forecast for the next three months (see last paragraph of summary).

Colin Mowl

COLIN MOWL

PUBLIC SECTOR BORROWING

Summary

- The PSBR in December was £0.2 billion. Local authorities' borrowing was unusually high compared with December in earlier years.

- Borrowing for April to November has been revised up by £0.4 billion.

- Borrowing is continuing to run well below the levels expected at the time of the Budget. The PSBR for the first nine months of 1987-88, at a surplus of £0.4 billion, is £5.6 billion below the Budget profile, mainly accounted for by lower central government own account borrowing.

- Excluding privatisation proceeds the April - December outturn is about £2¾ billion lower than the corresponding period last year and about £5 billion below the Budget profile.

- The usual forecasts for the PSBR in the next three months are not presented in this note. A new forecast of the PSBR in 1987-88, taking into account the prospects for January to March, will be included in the Treasury winter economic forecast.

Figures in this report are not seasonally adjusted and also may not sum precisely because of rounding.

Chart 1 : 1987-88: Comparisons with 1987 Budget profiles

£ billion cumulative

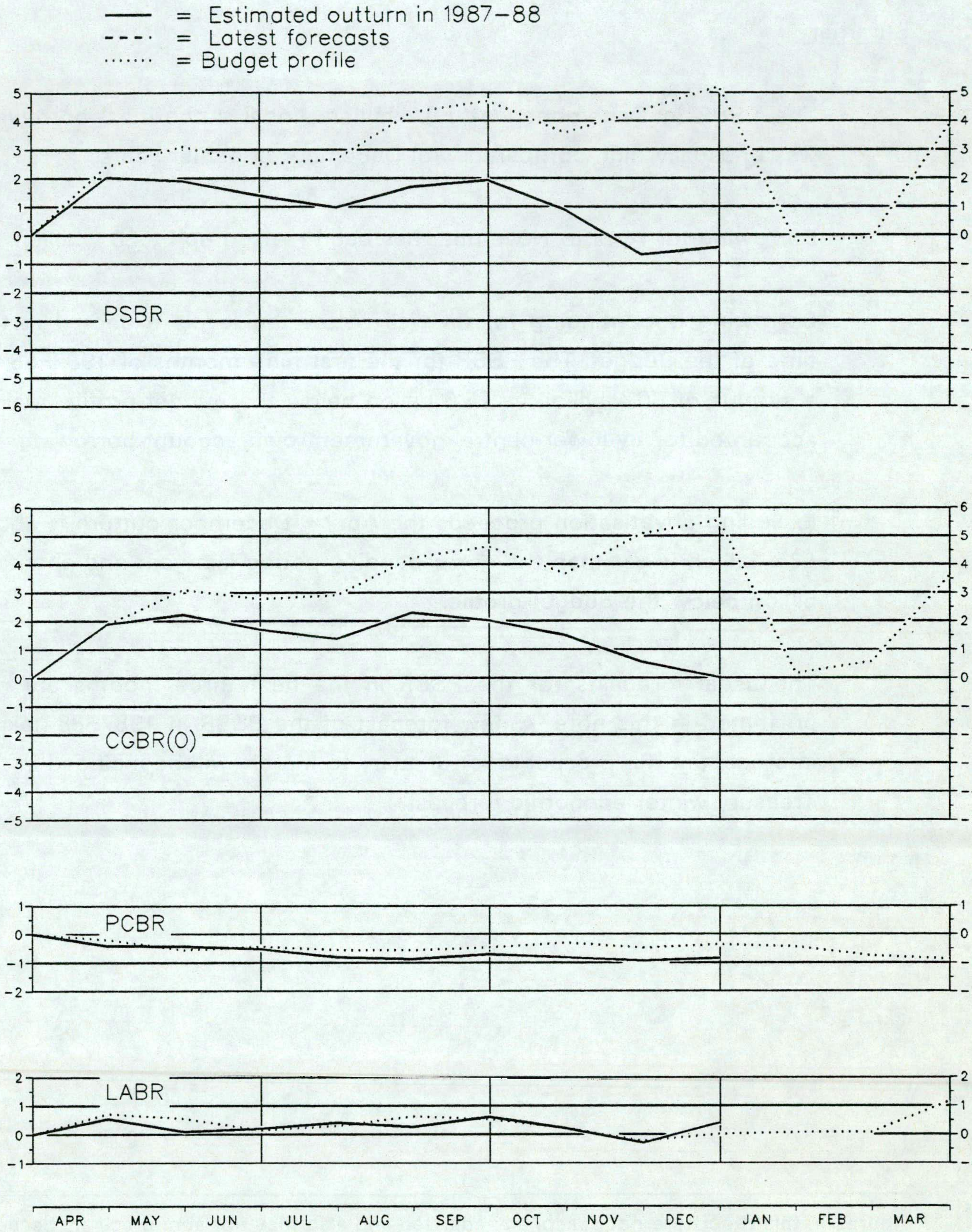


Chart 2: 1987-88: Comparisons with outturns for 1986-87

£ billion cumulative

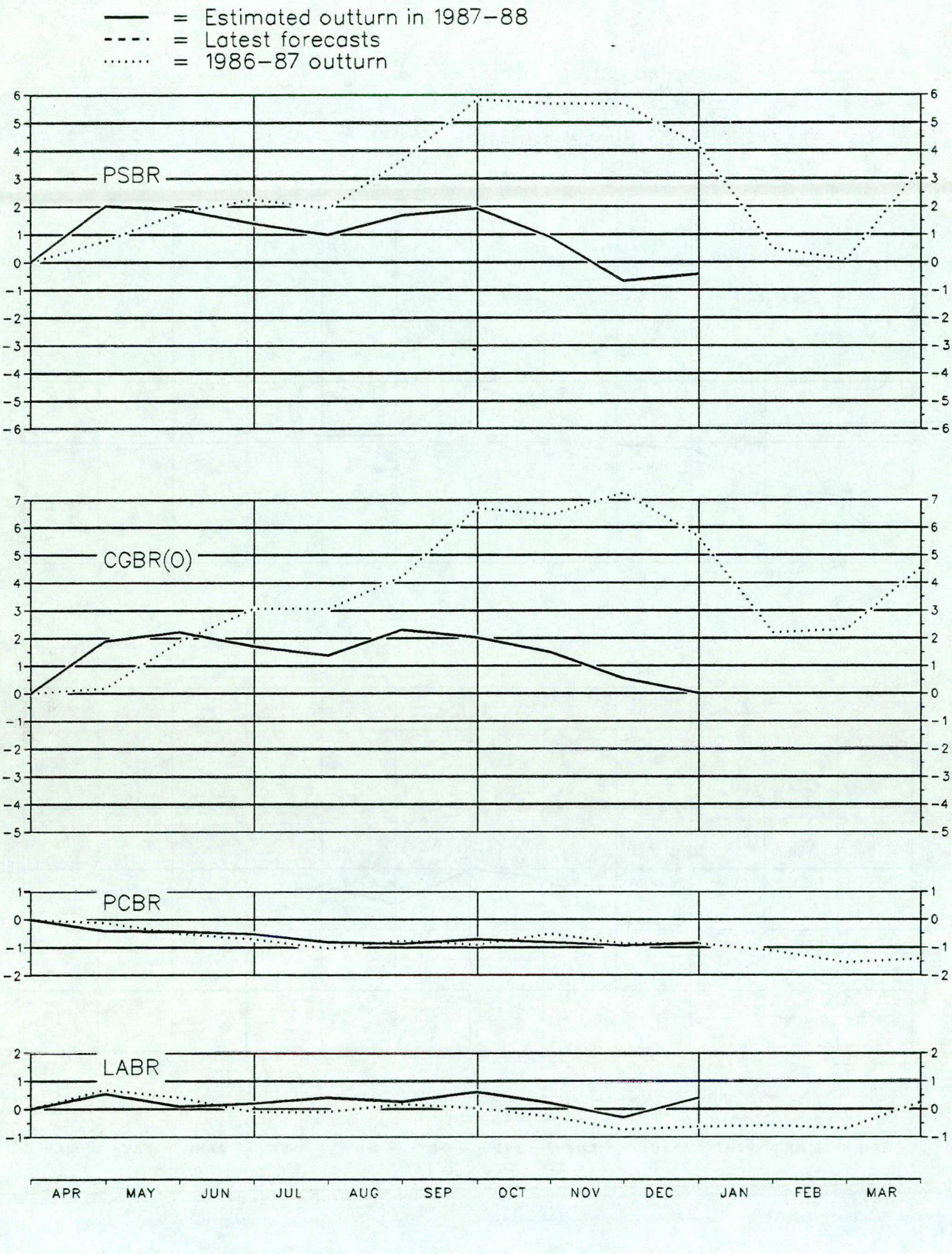
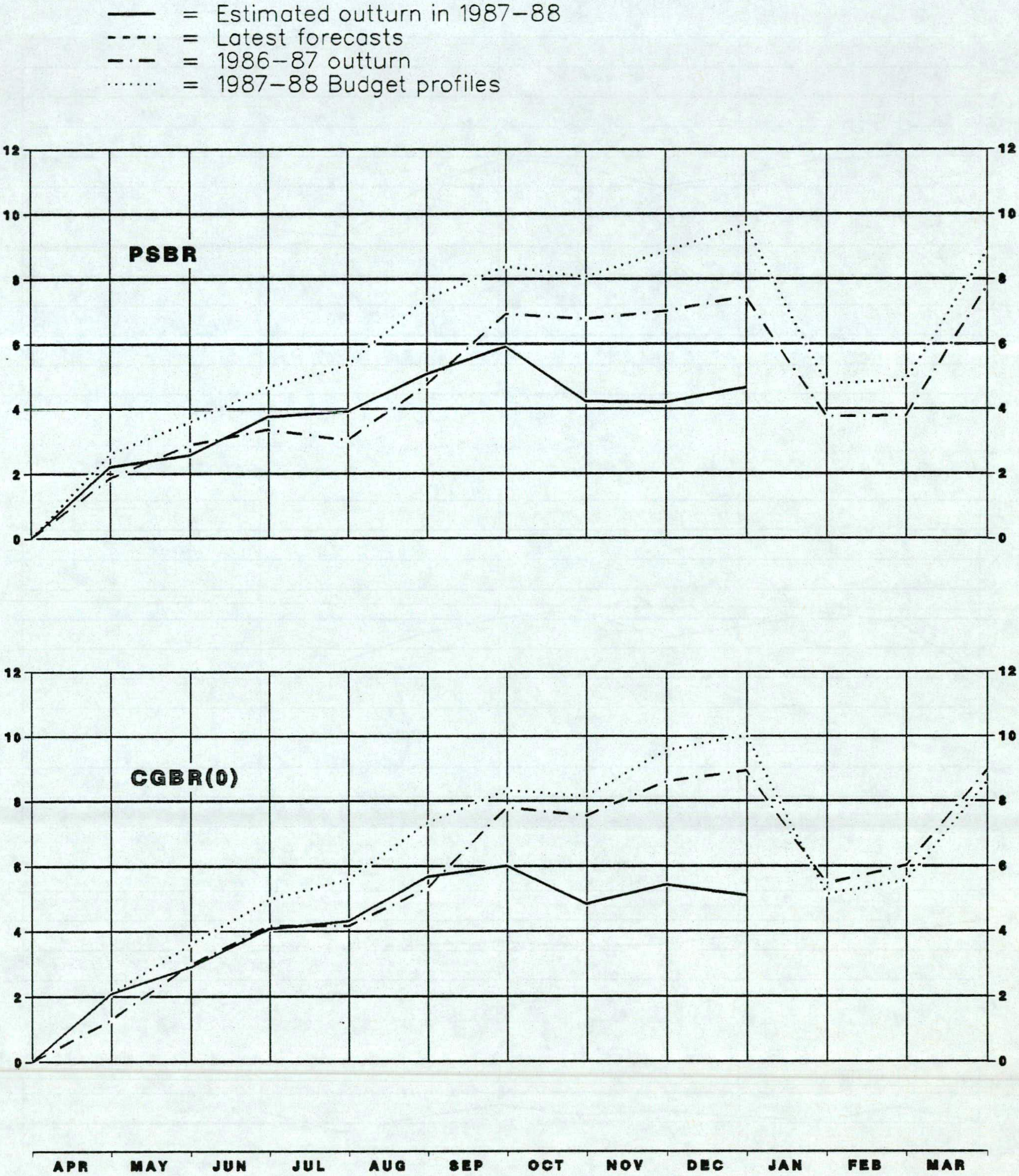


Chart 3: Comparisons excluding privatisation proceeds

£ billion cumulative



Borrowing in December

(Outturn compared with last month's forecast)

1. The provisional estimate of the PSBR in December is £0.2 billion. As shown in the table below the provisional outturn was £0.3 billion lower than the forecast made a month ago, with overforecasts of the CGBR(O) and PCBR partly offset by an underforecast of the LABR.

Table 1: December 1987 borrowing requirements

£ billion

	PSBR	Comprising		
		CGBR(O)	LABR	PCBR
Forecast*	0.5	0.2	0.2	0.2
Outturn	0.2	-0.5	0.7	0.1
Difference	-0.3	-0.7	0.5	-0.1

*made on 16 December

2. There was a surplus on the central government's own account of £0.5 billion, compared with a forecast last month of borrowing of £0.2 billion. The difference was mainly the result of higher than expected Inland Revenue receipts (by £0.6 billion), due to higher than expected Corporation Tax (£0.3 billion) and Income Tax (by £0.3 billion) receipts. The higher Corporation Tax may be due to early payment of tax due in January, but it may alternatively reflect the unexpected buoyancy which has been a feature of the last year.

3. There was little effect on the CGBR(O) in December from the repurchase of BP shares. By the end of December some 17 million shares had been repurchased at a cost of £12 million. This cost has been netted off the December figure for privatisation proceeds. It is estimated that there have been a further 22 million shares repurchased at a cost of £15 million by the time the buy-back offer closed on 6 January. This will be reflected in the outturn for January.

4. Local authorities provisionally borrowed £0.7 billion in December, compared to forecast

borrowing of £0.2 billion. In nominal terms this is the highest ever recorded LABR in December. Local authorities borrowed £0.3 billion in December 1985 and £0.1 billion in December 1986.

5. Public corporations' borrowing requirement (PCBR) in December is provisionally £0.1 billion, compared to forecast borrowing of £0.2 billion. A full industrial breakdown of the PCBR is not yet available. British Coal, British Shipbuilders and "other" public corporations have all borrowed less than forecast. However, this has been offset by the Electricity Council, British Rail, the Civil Aviation Authority and the North of Scotland Hydro-Electric Board, who have all borrowed more than forecast.

April to December

6. The cumulative PSBR for the first nine months of 1987-88 was a surplus of £0.4 billion, £5.6 billion below the Budget profile (see chart 1 and Table 2) and £4.6 billion below the first nine months of 1986-87. Excluding privatisation proceeds the PSBR so far this year is £5 billion below the Budget profile and £2¾ billion lower than the equivalent period last year.

Table 2: Total April-December borrowing requirements

£ billion

	PSBR	Comprising		
		CGBR(O)	LABR	PCBR
Budget forecast	5.2	5.5	-	-0.4
Outturn	-0.4	-	0.4	-0.8
Difference	-5.6	-5.5	0.4	-0.5

7. Cumulative borrowing in April to December on the central government's own account was £5.5 billion lower than the Budget profile. Four fifths of the undershoot of the Budget

profile is accounted for by higher receipts and one fifth by lower expenditure. Table 3 shows differences on individual components have occurred.

Table 3: CGBR(O) April – December: Differences from Budget profile

	£ billion	percentage difference
Receipts		
Inland Revenue	+2.9	+7.2
Customs and Excise	+0.4	+1.4
NICs	+0.2	+0.8
Privatisation proceeds	+0.6	+13.5
Interest and dividends	−0.2	−3.1
Other receipts	+0.5	+16.7
Total receipts	**+4.4**	**+4.1**
Expenditure		
Interest payments	−0.2	−1.4
Departmental expenditure [1]	−1.0	−1.0
Total expenditure	**−1.2**	**−1.1**
Net effect on CGBR(O)	**−5.5**	

[1] on a cash basis, net of certain receipts and on-lending

8. The main factors reducing borrowing are:

- higher Inland Revenue receipts, mainly due to higher Corporation Tax (£1.2 billion), including ACT (£0.3 billion) and North Sea MCT (£0.1 billion). Income tax is £0.9 billion higher, with higher PAYE partly offset by lower than expected other income tax. PRT and stamp duties are respectively about £0.2 billion and £0.4 billion higher than forecast at Budget time.

- higher Customs and Excise receipts,mainly VAT. Higher than expected Keith effects may have contributed something to the higher than expected VAT, but the main explanation is probably higher consumer spending on goods and services subject to VAT - which does not yet appear to have been reflected in the official expenditure figures. Other Customs and Excise duties are slightly lower than forecast at Budget time.

- higher national insurance contributions.

- higher privatisation proceeds, mainly higher than expected receipts from Rolls Royce and earlier receipt than forecast of redemption of BT preference shares.

- higher other receipts, £0.3 billion of which is due an increase in the balances held on behalf of the European Community.

- A shortfall on departmental expenditure (measured on a cash basis) of about £1.0 billion. This is not fully reflected in expenditure returns by departments (the APEX returns), which show supply expenditure £0.5 billion below budget profile. However, there are definitional and timing differences between the APEX and cash measurements. On the APEX measure the main programmes which are below profile are defence, overseas aid, employment, social security and grants to British Rail. The main programmes above profile are ECGD's trading account, health and payments to British Coal.

9. After taking account of an upward revision of £0.5 billion to the LABR for April to November the local authority borrowing requirement in April to December is £0.4 billion. The December outturn and revisions to earlier months have changed the picture compared with that in recent notes. Previously the LABR had been running well below the Budget profile, though at much the same levels as 1986-87. Now it is £0.4 billion above profile and £1 billion above the level of the first nine months of 1986-87.

10. The cumulative PCBR for the first nine months of 1987-88 is a surplus of £0.8 billion, compared to a Budget forecast of a surplus of £0.4 billion. Table 4 shows cumulative borrowing to December (or to November where no December figures are yet available) for the PCBR and selected public corporations, excluding those privatised since 1 April 1986. Borrowing estimates for individual corporations are provided by the corporation themselves, and are not necessarily fully consistent with the aggregate PCBR estimates which are

based on information available within central government and from the banks. British Coal, the Electricity Council, British Steel, the Post Office, Water and "other" public corporations have all borrowed less than last year and less than was forecast at Budget time.

Table 4: Public Corporations' borrowing April–December

£million (–indicates lower borrowing)

	Difference from 1986-87	Difference from Budget profile⁺
Coal	–	-70
Electricity	-60	-20
British Steel	-80*	-70*
Post Office	-60*	-120*
Water	-160*	-30*
Other NIs	-280*	20 *
Other PCs	-260	-220
PCBR	-990**	-450**

*No December figure yet available figures cover April- November only

**Excluding industries privatised during 1986-87 and 1987-88

⁺components do not sum to total difference in PCBR, because of incomplete information on borrowing in December.

Chart 4: Components of central government receipts and expenditure

£ billion

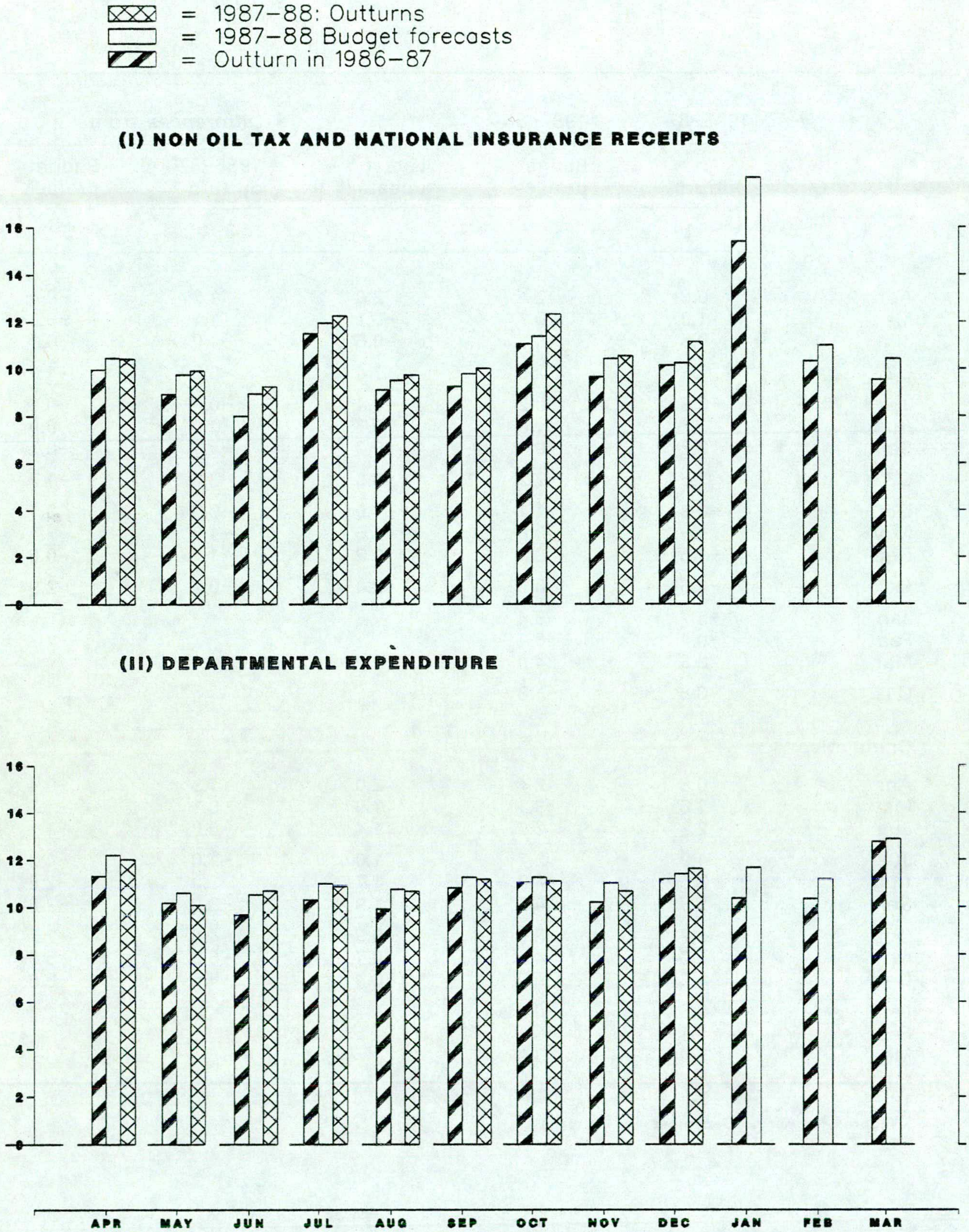


Table 5: PSBR for 1987-88 - comparisons with 1986-87 and 1987 Budget profile

£ billion

	1986-87	1987-88		Differences from	
	Outturn	Budget profile	Latest update[1]	1986-87 outturn	Budget profile
	1	2	3	3-1	3-2
Apr	0.8	2.4	**2.0**	1.3	-0.4
May	1.0	0.7	**-0.1**	-1.1	-0.8
Jun	0.5	-0.6	**-0.5**	-1.0	0.1
Q2	2.3	2.5	**1.4**	-0.9	-1.1
Jul	-0.3	0.2	**-0.4**	-0.1	-0.6
Aug	1.7	1.6	**0.7**	-1.0	-0.9
Sep	2.2	0.4	**0.2**	-1.9	-0.2
Q3	3.6	2.2	**0.5**	-3.0	-1.7
Oct	-0.2	-1.1	**-1.0**	-0.9	0.1
Nov	-	0.8	**-1.6**	-1.6	-2.4
Dec	-1.5	0.8	**0.2**	1.7	-0.6
Q4	-1.6	0.5	**-2.4**	-0.7	-2.9
Jan	-3.7	-5.4			
Feb	-0.4	0.1			
Mar	3.3	4.0			
Q1	-0.8	-1.3			
Cumulative					
Apr	0.8	2.4	**2.0**	1.3	-0.4
May	1.8	3.1	**1.9**	0.1	-1.2
Jun	2.3	2.5	**1.4**	-0.9	-1.1
Jul	1.9	2.7	**1.0**	-1.0	-1.7
Aug	3.6	4.3	**1.7**	-2.0	-2.6
Sep	5.8	4.7	**1.9**	-3.9	-2.8
Oct	5.7	3.6	**0.9**	-4.8	-2.7
Nov	5.7	4.4	**-0.7**	-6.3	-5.0
Dec	4.2	5.2	**-0.4**	-4.6	-5.6
Jan	0.5	-0.2			
Feb	0.1	-0.1			
Mar	3.4	3.9			

[1]Figures for April - December are outturns

Table 6: Borrowing requirement monthly profiles April-December, 1987-88

(Budget profiles in italics for comparison) £ billion

	PSBR		CGBR(O)		LABR		PCBR	
Apr	**2.0**	*2.4*	**1.9**	*1.9*	**0.5**	*0.7*	**-0.4**	*-0.2*
May	**-0.1**	*0.7*	**0.3**	*1.2*	**-0.5**	*-0.2*	**-**	*-0.4*
Jun	**-0.5**	*-0.6*	**-0.5**	*-0.3*	**0.1**	*-0.4*	**-0.1**	*0.1*
Jul	**-0.4**	*0.2*	**-0.3**	*0.1*	**0.2**	*0.2*	**-0.3**	*-0.1*
Aug	**0.7**	*1.6*	**0.9**	*1.3*	**-0.2**	*0.3*	**-0.1**	*-*
Sep	**0.2**	*0.4*	**-0.3**	*0.4*	**0.4**	*-0.1*	**0.2**	*0.1*
Oct	**-1.0**	*-1.1*	**-0.5**	*-1.0*	**-0.4**	*-0.3*	**-0.1**	*0.2*
Nov	**-1.6**	*0.8*	**-0.9**	*1.4*	**-0.5**	*-0.5*	**-0.1**	*-0.2*
Dec	**0.2**	*0.8*	**-0.5**	*0.5*	**0.7**	*0.2*	**0.1**	*0.1*
Cumulative								
Apr	**2.0**	*2.4*	**1.9**	*1.9*	**0.5**	*0.7*	**-0.4**	*-0.2*
May	**1.9**	*3.1*	**2.2**	*3.1*	**0.1**	*0.6*	**-0.4**	*-0.6*
Jun	**1.4**	*2.5*	**1.7**	*2.8*	**0.2**	*0.1*	**-0.5**	*-0.4*
Jul	**1.0**	*2.7*	**1.4**	*2.9*	**0.4**	*0.3*	**-0.8**	*-0.6*
Aug	**1.7**	*4.3*	**2.3**	*4.2*	**0.3**	*0.6*	**-0.9**	*-0.6*
Sep	**1.9**	*4.7*	**2.0**	*4.6*	**0.6**	*0.5*	**-0.7**	*-0.5*
Oct	**0.9**	*3.6*	**1.5**	*3.7*	**0.2**	*0.2*	**-0.8**	*-0.3*
Nov	**-0.7**	*4.4*	**0.6**	*5.1*	**-0.3**	*-0.2*	**-0.9**	*-0.5*
Dec	**-0.4**	*5.2*	**-**	*5.5*	**0.4**	*-*	**-0.8**	*-0.4*

	Excluding privatisation proceeds				Memo item:	
	PSBR		CGBR(O)		privatisation proceeds	
Apr	**2.2**	*2.6*	**2.1**	*2.1*	**0.2**	*0.2*
May	**0.4**	*1.0*	**0.8**	*1.5*	**0.5**	*0.3*
Jun	**1.2**	*1.1*	**1.2**	*1.4*	**1.7**	*1.7*
Jul	**0.2**	*0.7*	**0.2**	*0.6*	**0.6**	*0.5*
Aug	**1.1**	*2.0*	**1.4**	*1.7*	**0.4**	*0.4*
Sep	**0.9**	*1.0*	**0.3**	*1.0*	**0.6**	*0.6*
Oct	**-1.7**	*-0.3*	**-1.2**	*-0.2*	**-0.6**	*0.8*
Nov	**-**	*0.8*	**0.6**	*1.4*	**1.5**	*-*
Dec	**0.4**	*0.8*	**-0.3**	*0.5*	**0.2**	*-*
Cumulative						
Apr	**2.2**	*2.6*	**2.1**	*2.1*	**0.2**	*0.2*
May	**2.6**	*3.6*	**2.9**	*3.6*	**0.7**	*0.5*
Jun	**3.8**	*4.7*	**4.1**	*5.0*	**2.4**	*2.2*
Jul	**3.9**	*5.4*	**4.3**	*5.6*	**2.9**	*2.7*
Aug	**5.1**	*7.4*	**5.7**	*7.3*	**3.4**	*3.1*
Sep	**5.9**	*8.4*	**6.0**	*8.3*	**4.0**	*3.7*
Oct	**4.2**	*8.1*	**4.8**	*8.2*	**3.3**	*4.5*
Nov	**4.2**	*8.9*	**5.4**	*9.6*	**4.9**	*4.5*
Dec	**4.7**	*9.7*	**5.1**	*10.0*	**5.1**	*4.5*

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TABLE 7

CENTRAL GOVERNMENT TRANSACTIONS - DECEMBER OUTTURN

£ billion

	December		
	Forecast	**Outturn**	**Difference**
Receipts			
Inland Revenue	4.7	5.3	0.6
Customs and Excise	3.9	3.8	-0.1
National Insurance Contributions	2.1	2.0	-0.1
Privatisation proceeds	0.2	0.2	-
Interest and dividends	0.7	0.8	0.1
Other receipts	0.8	0.8	0.1
Total Receipts	12.2	12.9	0.6
Expenditure			
Interest payments	0.7	0.7	-
Departmental expenditure (a)	11.7	11.7	-
Total expenditure	12.4	12.3	-0.1
CGBR(O)	0.2	-0.5	-0.7
CGBR(O) excluding privatisation proceeds	0.3	-0.3	-0.6
On-lending to LAs	0.1	-0.1	-0.2
On-lending to PCs	-0.1	0.2	0.3
CGBR	0.2	-0.5	-0.6

(a) on a cash basis, net of certain receipts

\+ = higher receipts, and higher borrowing, higher expenditure
\- = lower receipts, and lower borrowing, lower expenditure

CONFIDENTIAL

TABLE 8

CENTRAL GOVERNMENT TRANSACTIONS - CUMULATIVE
DIFFERENCES FROM BUDGET PROFILES

£ billion

	Difference in outturn April-December	
	£ billion	Percentage difference
Receipts		
Inland Revenue	2.9	7.2
Customs and Excise	0.4	1.4
National Insurance Contributions	0.2	0.8
Privatisation proceeds	0.6	13.5
Interest and dividends	-0.2	-3.1
Other receipts	0.5	16.7
Total Receipts	4.3	4.1
Expenditure		
Interest payments	-0.2	-1.4
Departmental expenditure (a)	-1.0	-1.0
Total expenditure	-1.2	-1.1
CGBR(O)	-5.5	..
CGBR(O) excluding privatisation proceeds	-4.9	..
On-lending to LAs	1.7	..
On-lending to PCs	-0.3	..
CGBR	-4.1	..

(a) on a cash basis, net of certain receipts

\+ = higher receipts, and higher borrowing, higher expenditure
\- = lower receipts, and lower borrowing, lower expenditure

3783/6

CONFIDENTIAL AND PERSONAL

TABLE 9:

CONSOLIDATED FUND REVENUES - % changes on year earlier

	FORECAST FOR 1987-88		APRIL-DECEMBER 1987			
	(i) FSBR(a)		(ii) FSBR		(iii) Outturn	
1. Total Inland Revenue	7		4		11	
of which: Income Tax		3½		3½		7½
Corporation Tax (d)		20½		5½		22½
North Sea taxes (c)		-16½		-12½		5½
Other (Stamp Duties and Capital Taxes)		13½		11		25½
2. Customs and Excise	6½		6		7½	
of which: VAT		9		7½		11½
Specific Duties		3		3½		1½
Other (e)		7½		7½		10
3. Vehicle Excise Duty	-½		3		4½	
4. Asset Sales	14		37½		56	
5. Other Consolidated Fund Revenue*	-16		-16½		3½	
6. Timing Adjustment (f)	64½		100		-85	
7. **TOTAL CONSOLIDATED FUND REVENUE**	5½		5½		10½	
Memorandum Items:						
Non North Sea Taxes		7		5		9½
North Sea Oil Taxes and Royalties		-13½		-9½		4

* This includes oil royalties, EC refunds, coinage receipts and CFERs.

(a) using 1986-87 outturn as a base
(b) using 1986-87 outturn as a base
(c) Payments of PRT, advance PRT and North Sea corporation tax but excluding royalties
(d) Includes onshore and North Sea ACT
(e) Includes difference between receipts and payments to Consolidated Fund for April to December
(f) Reflects privatisation proceeds paid initially to Paymaster General and then to Consolidated Fund

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pw

SECRET AND PERSONAL

1. Alex ✓

2. pmp

[by the way, Carys rang to ~~regret~~ ask if other depts' copies of timing letter to PG wd have been received yet. On reflection she wished CST had been first to tell star chamber members. Too late! M.

~~[for CST bilaterals]~~ CST.

discuss with

FROM: J MACAUSLAN

DATE: 21 JANUARY 1988

CHIEF SECRETARY

cc: Chancellor
Mr Anson
Mr Monck
Mr Phillips
Mr Turnbull
Mr Gieve
Mr Call

MEETING OF STAR CHAMBER: MONDAY 24 OCTOBER

You are meeting the members of the Star Chamber on Monday 24 October. I attach a speaking note. I also attach a half-updated summary of agreed settlements. (The figures in it do not reflect the impact of the new economic assumptions).

2. I have assumed that you will want to speak at respectable length, appear to give quite a lot of information, but stop well short of giving a clear picture of the outcome. But you may want to take the opportunity to

(a) note that colleagues have offered to make substantial savings or cuts in bids, and that there are some favourable developments eg lower unemployment and higher receipts.

(b) give some hints that the outcome will be consistent with Cabinet remit but that economic developments since July mean that remit must be interpreted strictly.

(c) explain that such an outcome is essential.

(d) mobilize support for policy decisions taken and against any attempts by other Cabinet colleagues to reopen.

3. You may want to steer the discussion that will, I suppose, ensue into safe channels - for instance, the line the Opposition may take on public expenditure, in the debate on Tuesday and in the period up to Christmas; how E(ST) worked; etc.

4. You may want to take with you your minute of 14 October to the Prime Minister about science and technology. Since colleagues have already seen that, you can safely draw on it as much as you like. If you expext to mention child benefit, you may want to take some of your social security briefing.

JM

J MACAUSLAN

gep1.ip/jm/spk St Ch

SECRET

SPEAKING NOTE FOR STAR CHAMBER

Most grateful to you all for sparing the time to meet.

[~~Not yet clear if~~/Expect not to have to] call you to meet, as it were, in anger. ?

Very pleased to have opportunity to sketch where we have got to.

In recent years, have achieved steady and substantial growth of public spending well within growth rate of economy. Means ratio of GGE to GDP has been declining, from peak of 46¾ per cent in 1982-83. At same time, public spending in real terms this year 18 per cent higher than when we took office.

Moreover, as economy improves, and with consistent adherence to sound financial policies, gradually able to target expenditure more on priority services.

Hence Cabinet remit to sustain that approach: to stick as close as possible to existing planning totals; and to ensure GGE continues to decline as a proportion of GDP.

A demanding remit. GGE ratio this year will have fallen a lot, due to very strong growth of economy. Not easy to continue the declining path from that point. And sticking close to planning totals is never easy. This year, particular difficulty due to substantial pre-existing commitments: decision to increase provision for local authority current expenditure by £1.6 billion in 1989-90; effects on expenditure of April decisions to modify new social security regime; knock-on effects of 1988 health Review Body awards; and higher payments to the EC. On top of that, massive bids from colleagues.

But developments in economy since July indicate that must take a strict interpretation of that remit. Increase in inflationary pressures very worrying. At time when we are seeking to restrain private spending through higher interest rates, totally inappropriate to be easing up on public spending.

Not yet clear where we will end up. Virtually all major policy issues on programmes now settled bilaterally, though still a good deal of work to settle ~~to~~ precise figures. October economic assumptions still to be dealt with. And of course major issues like size of Reserves, privatisation proceeds, debt interest. Expect to end up within remit. Hope to sort out within next few days.

I'll sketch major changes in programmes so far.

Large additions on net payments to EC. Due to Brussels package; also the strength of economy increases contributions. I've mentioned local authority current and health Review Body awards. Have also agreed significant further sums for health. Big upward estimating changes on social security: continuing increase in benefits for disabled - a particular problem - on which recent OPCS review relevant. Have agreed a package with John Moore under which child benefit will be frozen but part of savings will be used to boost Family Credit and Income Support. I believe this is entirely the right direction in which to move. Are courageous decisions which deserve our full support. But, with some relief from falling unemployment, have got social security programme just below baseline in the first year, which is an achievement. Falling unemployment has also helped on Employment programmes, as Norman knows. make a bit nicer, more grateful.

Upward Statement

Snub! Soc. Sec. prog

On nationalised industries, huge problem of loss of negative External Financing Limits in, in particular, 1991-92. Electricity and Water industries are big net repayers of debt. So, while in public sector, reduce planning total. When privatised, these repayments change their nature and are transferred out of public expenditure. Apart from that, the strong performance of nationalised industries has allowed more investment, while sticking near to baseline.

More money for science and universities in Education programme. 20 per cent increase for basic science between 1988-89 and 1989-90. Despite best efforts of Secretaries of State for Energy and Agriculture additions exceed savings we have been able to secure particularly in the early years.

eh?

Also increase on law and order: inevitable in view of concern, eg at Conference. Have also agreed a major addition for roads programme.

Substantial

But reductions on agricultural market support, and extra Right to Buy receipts have helped to make some dent in the resulting increases. We will be able to demonstrate a qualitative improvement in our spending plans. In last Survey and this have been able to devote more resources where we want them to go rather than where circumstances dictate.

Negotiations have been tough, as you all know, and as most of you have experienced at first hand. But colleagues have been constructive, and have in recent bilateral discussions offered significant savings to help soften the impact on the totals of the massive increases bid for.

But, on the other hand, market sensitivity much greater than at the start of the round, with greater fears on inflation front and on current account. All the more need to keep to the Cabinet remit.

1 BAP Benefits
Bene Plans
swallowing up
by higher EC
contributions

gep1.ip/jm/bids

ANNEX B

SECRET AND PERSONAL

SUMMARY OF AGREED PROGRAMMES

CMO UNTIL 31/12/1988

[illegible]

	1989-90	1990-91	1991-92
			£ million
Defence	+ 100	+ 500	+ 900

Increased provision is offset in part by higher efficiency and other savings.

FCO (diplomatic wing)	+ 21	+ 42	+ 46

Increases for scholarships and exchanges, running costs, BBC External services grant, security measures and new technology are offset in part by favourable overseas price movements and savings on broadcast relay stations.

ODA	+ 30	+ 69	+ 94

The increases provide for the expected costs of the sub-Saharan debt initiative, and for the UK's contribution to the IMF ESAF; the settlement also provides additions to bilateral aid including ATP soft loans.

EC Contributions	+ 500	+ 630	+ 230

EC contributions

The sharp increase in the net contributions in 1989-90 and 1990-91 is a result of the Brussels agreement on the future financing of the Community, the buoyancy of imports, and upwards revisions to our VAT payments and our share of the new GNP - based fourth resource.

IBAP	- 421	- 396	- 268

The reductions are due to revised forecasts of UK harvests and of the impact of CAP reform measures. There is also some benefit from poor harvests in US. The projections make some allowance for future devaluation of the Green Pound.

<u>Other agriculture</u>	+ 15	+ 9	+ 5

Increases for running costs, flood prevention, and other programmes are offset in part by estimating and policy reductions in capital grants, and by savings from increased funding by industry of R and D and ADAS.

<u>DTI</u>	+ 64	+ 79	- 72

There are increases for regional assistance, assistance to shipbuilding, and for running costs and major works (mainly reflecting relocation plans). These increases are offset in part by reductions on support for innovation, and, in 1991-92, by the run down of existing launch aid commitments.

<u>Energy</u>	+ 36	+ 5	- 71

The changes result mainly from decisions on nuclear R&D programmes, notably to run down the fast reactor and fusion programmes, which generate redundancy and restructuring costs as well as savings. Further estimating savings arise on the Redundant Mineworkers Payments Scheme.

<u>Employment</u>	- 200	- 300	- 400

Savings result from the rapid fall in unemployment and from the declining number of school leavers.

<u>Environment</u>	- 1208	- 1068	- 769

Increased projections of receipts will yield some £4 billion over the three years. There are additions of around £400 million a year to gross capital spending on housing and for the Urban block, and for the costs of preparation for the Community Charge.

<u>Transport</u>	+ 324	+ 398	+ 406

PSA	+ 28	+ 16	- 29

A combination of higher receipts from disposals and net rents and modest additions to the net baseline in 1989-90 and 1990-91 will enable the PSA to meet foreseeable requirements for major works, to continue to reduce the maintenance backlog and to invest in improved management structures, working towards full payment and untying in 1990 and Trading Fund status by 1993.

Home Office	+ 246	+ 354	+ 324

There are increases for prison building and prison manpower, and smaller increases for a range of non-prisons spending, offset by higher local authority capital receipts and other savings.

Lord Chancellor's Department and other legal	+ 34	+ 61	+ 106

There are increases for legal aid, running costs, and court building; and for the Serious Fraud Office; and for the Crown Prosecution Service, particularly in 1991-92.

Education	+ 359	+ 400	+ 364

The agreed additions provide for a real increase of some 10 per cent in the Science budget between 1988-89 and 1989-90; put the polytechnics and colleges on a sound footing for their new, independent status; allow the value of student awards to be maintained; and provide for £352 million capital allocations for local education authorities in England which will allow a continued programme of school improvements.

Arts and Libraries	+ 4	+ 2	+ 20

The settlement rolls forward the three-year programme agreed in the 1987 survey (with increases in the new third year, for example for incentive funding); and provides for the construction programme for the British Library, St Pancras project.

Health and Personal Social Services	+ 1260	+ 1480	+ 1900

Increases reflect the knock-on costs of this year's Review Body awards, the effect of demographic and other developments on hospital activity and demand in the Family Practitioner Services, the growing cost of AIDS, and increased provision for capital expenditure on equipment and maintenance. The likely costs of Whitley pay settlements are included in the settlement. There are offsetting savings from efficiency improvements and from a reduction in employers' superannuation contributions.

Social Security	- 123	+ 1677	+ 3742

Child benefit freeze; extra 50p on child credits in family credit and child allowances in income support. Large estimating increases, especially in the later years, result from higher expenditure on disability benefits and income support, and from reductions in the benefit savings expected to be made as a result of the new Employment Training Programme. The cost of compensating benefit claimants for the average 20 per cent payment of community charge has increased. The changes agreed in April to housing benefit also require additions to provision. These increases are offset in part by the effects of reductions in unemployment. In addition, the Secretary of State has decided to find savings by making changes to some income support rules, recovering benefits from tort damage awards, and tightening up the unemployment benefit rules.

Scotland	+ 213	+ 259	+ 342

There is an increase to Scottish programmes of industrial assistance, particularly for the Scottish Development Agency. The settlement also provides for VAT on new construction on the Scottish block.

Wales	+ 172	+ 179	+ 204

Northern Ireland	+ 115	+ 136	+ 190

The settlement provides for an element of uplift in recognition of the particular pressures arising from the security situation in the province. The Chief Secretary also agreed that the Secretary of State could use the excess assets of the Northern Ireland Consolidated Fund to create some £50 million of additional spending power within the existing baseline.

Nationalised industries	- 4	- 12	+ 1374

Cabinet's remit to keep total provision to baseline or less is fulfilled in years 1 and 2. The whole of the additional provision in year 3 is accounted for by the loss of electricity industry's substantial negative EFLs after privatisation. Settlement provides for increased capital investment in water industry to meet EC and domestic requirement, partially offset by price increases of 9.8 per cent (cash). Large increases in London Regional Transport (LRT) to finance investment more than offset by reductions from baseline in other transport industries. LRT fares will rise by about 12 per cent (cash) and Network South-East fares by 3.6 per cent (in real terms). Electricity prices will rise around 6 per cent (cash) in 1989-90.

Local authority relevant current	+1,653	+1,984	+2,211

Ministers have agreed in July to make provision for relevant current expenditure by local authorities in Great Britain which implies substantial increases over baseline. Figures for later years project forward the provision agreed for 1989-90 at a level constant in real terms.

016/2981

pmg

CHIEF SECRETARY TO THE TREASURY

FROM: JILL RUTTER

DATE: 22 January 1988

PS/CHANCELLOR

cc:
PS/FST
PS/PMG
PS/EST
Sir Peter Middleton
Mr Anson
Mr Kemp
Mr Turnbull
Mr Gieve
Mr Pickford
Mr R I G Allen
Mr Cropper
Mr Tyrie
Mr Call

PEWP: LETTER TO BACKBENCHERS

... I attach the final version of the letter to backbenchers which the Chief Secretary circulated today.

Jill Rutter

JILL RUTTER
PRIVATE SECRETARY

From: The Rt Hon John Major

HOUSE OF COMMONS
LONDON SW1A 0AA

22nd January 1988

Dear Colleague,

WHITE PAPER ON PUBLIC EXPENDITURE

The White Paper on Public Expenditure was published on Wednesday. I thought you might find it useful to have some background and key points on it.

The Public Expenditure White Paper is not an occasion for announcing new decisions on public expenditure. Those were announced last November in the Autumn Statement when the Chancellor set out our plans for increases both in the overall level of public spending and, particularly, on our priority programmes over the next three years.

The White Paper fleshes out those plans with further details on each individual programme. It explains exactly where the money goes, what it buys and how we are obtaining better value for money. It shows clearly how we have increased spending on our priorities. The two month delay between the announcement of our plans and the publication of the White Paper does not spring from any further review of plans, which occurs annually, but simply reflects the considerable practical task of collating the detailed information and producing a document of over 500 pages.

Looking at the totals first, our stated strategy remains - as it has been since 1979 - to reduce the public sector's share of total national income so that we can reduce taxation and provide a favourable climate for the private sector while maintaining a prudent level of borrowing. That is the way to foster enterprise and economic growth, without which we cannot improve public services and private prosperity on a sustainable basis.

In this way, as the economy grows we are able to afford real increases in public spending without putting a strain on the national finances. In the four years from 1986-87 to 1990-91 we plan for real terms growth in total expenditure of about 1¼ per cent a year. Within that sum the amount available for services is planned to increase more speedily because our prudent approach to borrowing is sharply reducing the growth in the burden of debt interest. In the next three years, therefore, the sums available for services are set to increase by over 2 per cent a year in real terms - over £3 billion a year extra at today's prices.

Each year we carefully re-examine spending plans, and the White Paper reflects the fact that in the last review we felt able to increase public expenditure plans for 1988-89 by £2½ billion (following an increase of £5½ billion for 1988-89 in last year's White Paper) and £5½ billion for 1989-90.

So the true message from our plans is that we have been able to increase priority expenditure within the framework of a prudent approach to public finances. Tax rates are down, borrowing is down, and priority spending is up. This prudent approach, of ensuring that total public expenditure grows less rapidly than the economy as a whole, was clearly spelt out in our election manifesto last year, and we will stick to it.

Keeping public spending under control does not mean arbitrary savings. But we have consciously made savings in a number of areas: reducing subsidies to industry, both public and private; by getting the private sector to play a greater role in housing; and by holding down borrowing. This has enabled us within our new plans to increase provision for a wide range of priority programmes including:

(i) **Aid.** We have increased provision by £32 million in 1988-89 and £63 million in 1989-90 and in addition we have agreed to provide funds towards the extra cost of contributions to the IMF structural adjustment facility to help the poorest debtor countries. The aid budget is set to increase in real terms in the next 3 years.

(ii) **Arts.** This year we concluded a special three-year settlement for the arts which allows for central government spending to rise in cash terms by some 27 per cent over the years to 1990-91.

(iii) **Defence.** We have increased provision by over £200 million in 1988-89 and nearly £500 million in 1989-90 over last year's plans. There has been some comment about the apparent real terms fall in spending provision between 1987-88 and 1988-89. But to get a true picture, it is necessary to take account also both of the real increase of 25 per cent since 1978-79, and of the fact that the Ministry of Defence will carry forward a substantial sum from this year's budget into next year to add to the new provision set out in the White Paper. Moreover by contracting out support services we are saving at least £40 million a year and even larger sums by bringing competition to bear on defence procurement.

(iv) **Education.** The plans show an increase in provision of over £600 million in 1988-89 and £800 million in 1989-90. This will provide extra resources for universities and science and enable us to increase still further the proportion of young people entering higher education. As you know, this proportion is already at record levels. We have also made available an additional £60 million for capital spending to improve school buildings and a further £61 million to assist universities in essential restructuring. The science budget too has been increased by £50 million.

(v) **Health.** The Health service has again been a prime beneficiary. Our plans show the largest ever increases to provision for the NHS. Next year we have made provision to spend over £1.1 billion more than we are doing this year, and there are similar increases in the following years. (This increase is, of course, measured after including in the 1987-88 figure the extra money made available during the course of the year. If you compare next year's plans with the original plans for 1987-88 set out in last year's White Paper, the increase is around £1.7 billion). Taking account of the resources released by cost improvement programmes and by the new schemes for generating income in the hospital service, resources for 1988-89 will rise by between 2½ per cent and 3 per cent in real terms. We also have an excellent record on capital spending with over £1 billion committed to capital schemes next year. Since 1978-79 we have increased the level of capital spending by over 35 per cent in real terms. Our plans will enable the NHS to continue to expand and improve patient care.

(vi) **Housing and Environment.** Receipts from council house and new town sales are running at record levels, and this White Paper shows a further rise in provision for gross capital expenditure. This increase amounts to nearly £400 million in 1988-89 and includes additional provision for estate action, renovation of local authority buildings, the housing corporation and housing action trusts. The provision for Urban Development Corporations has been increased by £70 million in both 1988-89 and 1989-90.

(vii) **Law and Order.** This has always been a priority and remains so. Next year we have provided an additional £240 million for the police and an extra £60 million to speed up the prison building programme and provide an additional 4,200 prison places by 1993. Overall the programme shows a real increase of 50 per cent since 1978-79 with further real growth to come.

(viii) **Social Security.** Our plans again provide for large increases of over £1 billion in each year of the Survey. The social security budget continues to grow in real terms despite the welcome fall in unemployment. This is largely because of the continuing growth in the cost of pensions and of benefits for the sick, the disabled and families.

(ix) **Trade and Industry.** Provision for DTI programmes shows increases of £280 million a year in each of the next two years. David Young has announced a radical restructuring of programmes, to focus assistance on small businesses and to move away from automatic grants. Even so, as the plans made clear, this has not involved reductions in provision for regional assistance.

(x) **Transport.** The White Paper makes additional provision for a major programme of bridge maintenance. Capital spending on motorways and trunk roads in England will be 30 per cent higher in real terms in 1988-89 than 1978-79

(xi) **Science and Technology.** The White Paper shows increased provision for civil science and technology of about £250 million in 1988-89 and 1989-90 compared with previous plans. As a result civil science and technology spending will go up by 3 per cent next year in real terms.

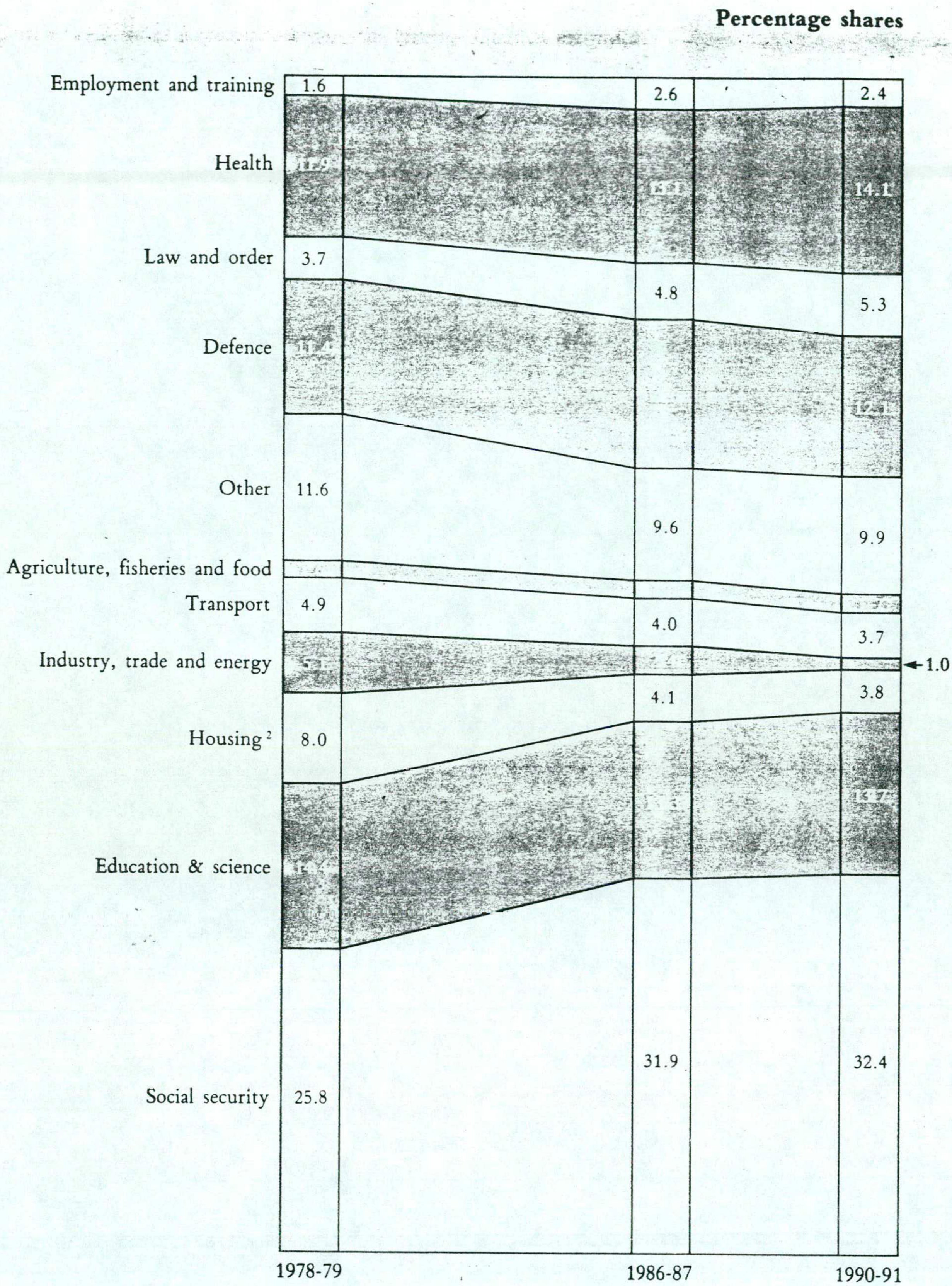
I attach a couple of charts from the White Paper which clearly illustrate our priorities and record on public spending. I hope you find this information useful and that it puts our plans in proper perspective.

Yours Ever,

John

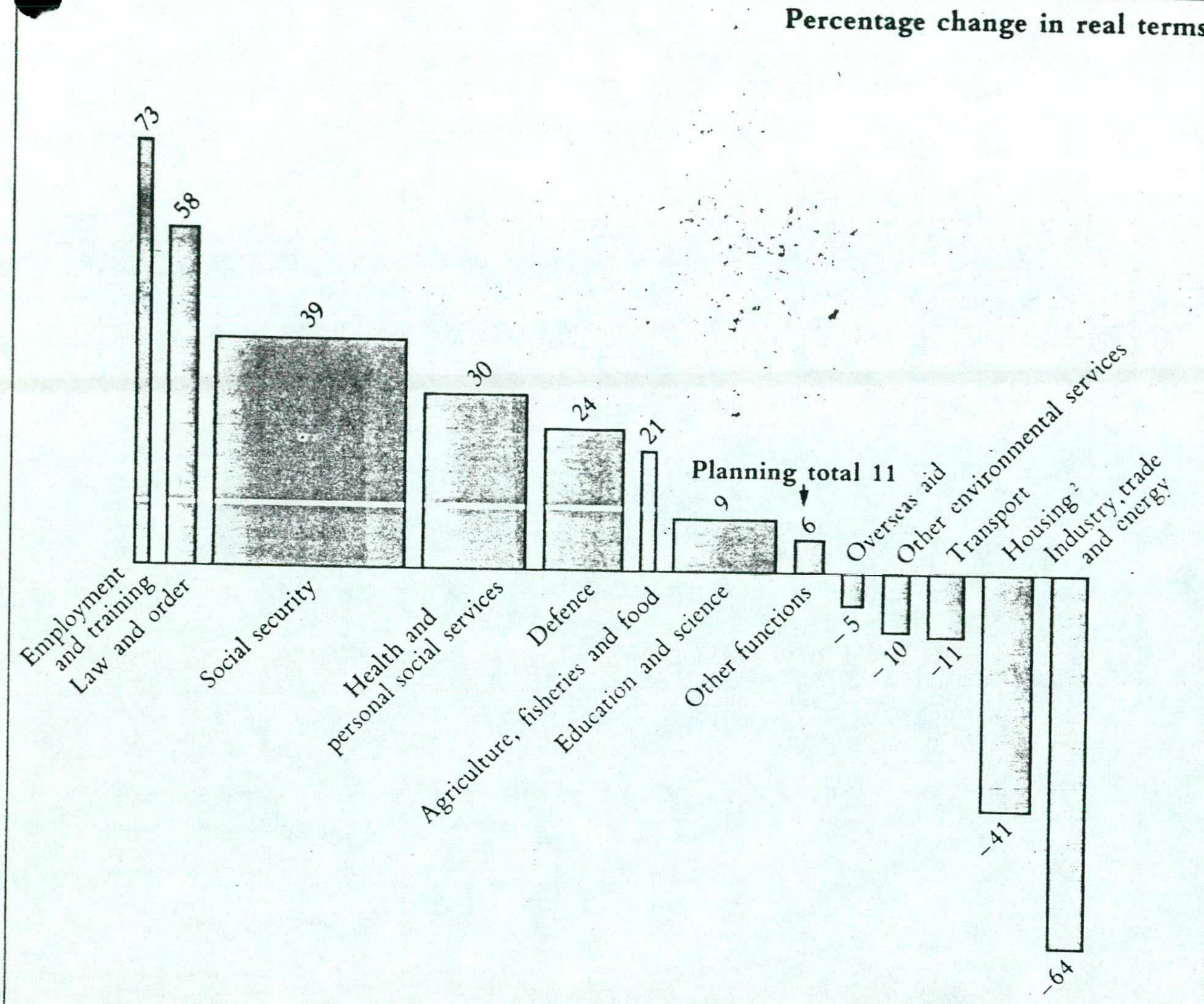
JOHN MAJOR

Chart 1.10 Public expenditure[1] by function



1. *Departmental spending ie excluding the Reserve and privatisation proceeds. Detailed figures are provided in Chapter 2, Table 2.7.*
2. *Gross of receipts.*

Chart 5.13 **Percentage changes in spending by function between 1978–79 and 1987–88**[1]



1. The width of each bar on the horizontal axis is proportional to the expenditure on that function in 1978 – 79

2. Housing figures are gross of receipts

13. **Table 5.14** illustrates trends in public sector capital spending. It uses the wider definition of capital spending described earlier and shows that public sector capital spending in the current year is broadly level, in real terms, with that in 1978–79.

35A/G/PC/8/28

pmp

FROM: R J DEVEREUX
DATE: 25 January 1988

1. MISS NOBLE

2. MR C D BUTLER

3. SIR PETER MIDDLETON

4. PAYMASTER GENERAL

5. Return to Vote Co-ordinator

[NR v. good!]

c c PS/Chancellor
Mrs Lomax
Mr Instone
Mr Hurst

SPRING SUPPLEMENTARY ESTIMATES 1987-88 : CLASS XIX, VOTE 12
Economic and financial administration : UK Coinage (HM Treasury)

This submission seeks your formal approval for a Supplementary Estimate of £6.0 million for the Coinage Vote. While a Supplementary of this size would normally be dealt with by Miss Noble, as a Treasury Vote it requires the approval of the Principal Finance Officer, the Accounting Officer, and the responsible Treasury Minister.

2. The vote covers expenditure by the Treasury made under contract to the Royal Mint for the manufacture and distribution of UK coins, and for the storage of withdrawn coins. The vote is not cash limited.

3. The recommended increase is £6.0 million, 41 per cent above the existing Main Estimate and PES provision, and involves an equivalent claim on the Reserve. There is no scope for offsetting savings and the claim on the Reserve was approved by Mr Anson on 21 January.

4. The risk of a supplementary on this vote was noted by Mr Hall last year when, with Minister's agreement, he arbitrarily cut the banks' forecasts of demand to keep the Main Estimate within the agreed PESC provision for 1987-88. At the time, he warned that if the banks proved right, it could require a supplementary estimate of at least £4.1 million. About 50 per

cent of coins are issued in the pre-Christmas period, and it is now clear that the position is rather worse than that expected. This is partly because the banks have asked for even more coins than their original forecast and partly because metal prices have risen very sharply in the last twelve months (see attached chart). An allowance for increased prices was included in the Main Estimate, but the final metal costs are still likely to be more than 30% above provision. It is also clear that the Appropriations-in-Aid shown in the Main estimate (from withdrawn coins) were too high.

5. I recommend that you approve a £6.0 million increase in provision on this vote, bringing the total provision to £20.6 million.

R J DEVEREUX

List of subheads

ANNEX A

'000

Subhead	Existing provision	Recommended increase
A1 (Coin issues)	16,850	3,748
A2 (Cost of storage)	250	75
AZ (scrap value of melted coins)	2,500	2,177
Net increase recommended for approval		6,000

Class XIX, Vote 12 Economic and financial administration: UK coinage (HM Treasury)

Introduction

1. Expenditure borne on this Vote is not subject to a cash limit.

2. Additional provision is sought for extra payments to the Royal Mint for the manufacture, storage and distribution of UK coins on behalf of the Treasury as a result of higher than expected demand for coins, and a sharp rise in metal prices.

3. Symbols are explained in the introduction to this booklet.

Part I **£6,000,000**

SUPPLEMENTARY amount required in the year ending 31 March 1988 for expenditure by the Treasury in connection with the manufacture and distribution of coinage for use in the United Kingdom.

The **Treasury** will account for this Vote.

Part II Summary and subhead detail

Summary

Present net provision		Changes proposed: Gross provision	Changes proposed: Appropriations in aid	Changes proposed: Net provision	New net provision
£'000		£'000	£'000	£'000	£'000
14,600*	**13.2 UK Coinage**	**~~3,800~~** 3823	**~~2,200~~** -2,177	**6,000**	**20,600**

*As in original Estimate (HC 227–XIX of 1987–88).

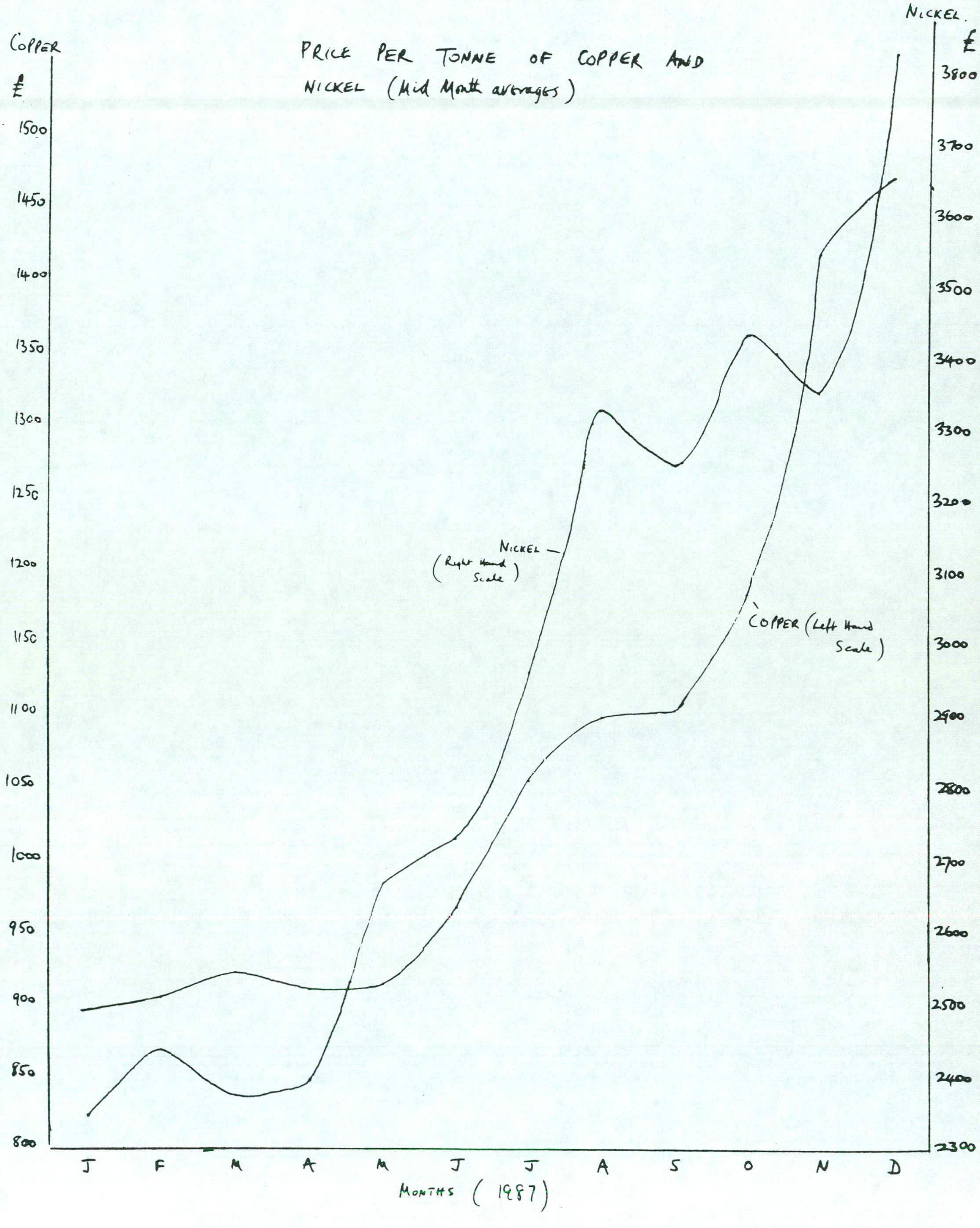
Subhead detail

Present provision		Increase/ excess	Decrease/ shortfall	New provision
£'000		£'000	£'000	£'000
16,850	**A1 United Kingdom coinage**	~~3,800~~ 3748	—	~~20,650~~ 20,598
	Less:			
2,500	**AZ Appropriations in aid** Proceeds of metal sales from melted down coins.	—	~~2,200~~ 2,177	~~300~~ 323
	Net total	3823	2,177	

Part III Extra receipts payable to the Consolidated Fund

As in existing provision.

250	A2 Incidental expenses Cost of storage, processing and other related expenses of handling returned coins	75	—	325



PRICE PER TONNE OF COPPER AND NICKEL (Mid Month averages)
COPPER
£
1500
1450
1400
1350
1300
1250
1200
1150
1100
1050
1000
950
900
850
800
NICKEL
£
3800
3700
3600
3500
3400
3300
3200
3100
3000
2900
2800
2700
2600
2500
2400
2300
NICKEL (Right Hand Scale)
COPPER (Left Hand Scale)
J F M A M J J A S O N D
MONTHS (1987)

CONFIDENTIAL

FROM: J S HIBBERD
DATE: 29 JANUARY 1988

CHANCELLOR OF THE EXCHEQUER

cc : Chief Secretary
Sir Peter Middleton
Sir Terence Burns
Mr Anson
Dame A Mueller
Mr Kemp
Mr Scholar
Mr Lankester
Mr Monck
Mr Burgner
Mr H P Evans
Mr Gilmore
Mr Mountfield
Mr Odling-Smee
Miss Peirson
Mr Peretz
Mr Robson
Mr Culpin
Mr Sedgwick
Mr Turnbull
Mrs R Butler
Mr Gieve
Mr Gilhooly
Mr MacAuslan
Mr McIntyre
Mr Mowl
Mr Allum
Mr Cunningham
Mr Call
Mr Cropper
Mr Tyrie

Ch
OK?
AA
OK

ECONOMIC ASSUMPTIONS FOR PUBLIC EXPENDITURE

Since the Anson report on Monitoring and Forecasting of Demand-led Expenditure, economic assumptions have been sent to Departments roughly once a quarter (in April, July, September/October and January). The January assumptions are usually the least important and are not regularly issued. In January 1986, for example, we did not circulate any revisions. In January 1987 we sent out revised assumptions only for unemployment and the RPI.

2. There is no pressing operational need for a general revision of assumptions now. The public expenditure planning total figures for 1988-89 and beyond will be the same as those in the PEWP. We shall undertake a comprehensive review of assumptions in April after the Industry Act Forecast and MTFS presented in the FSBR. If we issued revised assumptions now, we could then be faced with having to send substantial further revisions later. It seems best to avoid that possibility.

EcAssp
jan-87

3. There is a case, however, for sending DHSS in particular (but also DEmp, GAD and Northern Ireland Office) a revised unemployment assumption. The present assumption is significantly above the latest outturn. We have been strongly pressing the DHSS to improve their forecasting of social security, and there is advantage in doing what we can to assist in this process. If they feel that they are being asked to make calculations on unrealistic assumptions, they will not be encourage to improve their forecasting methods.

Unemployment

4. The PEWP assumption on GB adult unemployment was an average 2.7 million in 1987-88, followed by 2.6 million in 1988-89. However, unemployment figures in recent months have been better than expected when the PEWP assumptions were agreed in September.

5. Average unemployment for the whole of the current financial year now seems almost certain to come out close to 2.63 million; and we propose that the unemployment assumption for the current financial year should be revised to this figure. The latest figure for seasonally adjusted GB adult unemployment (for December) is just over 2.49 million. With prospects for further growth in output and employment, our current view is that GB adult unemployment could average around 2.3 million in 1988-89 (previous assumption 2.6). However, we would propose to issue a revised stylised working assumption of 2.4 million (the level we expect unemployment to reach by March 1988) for 1988-89 and beyond.

Unemployment Assumptions (GB Adult, millions)

	1987-88	1988-89	1989-90	1990-91
1988 PEWP	2.7*	2.6	2.6	2.6
Forecaster's current view	2.63	2.31	2.25	
Proposed revised assumptions	2.63	2.4	2.4	2.4

* This is the number departments are using, though it was not published in PEWP.

Decisions

Are you content for us to issue these revised assumptions? We would also circulate them to other departments (as we usually do), indicating, at the same time, that there are no other changes to assumptions.

Jim Hibberd

J S HIBBERD

LT

CONFIDENTIAL

MP

FROM: J. ANSON
2nd February, 1988.

CHANCELLOR

Many thanks. A most interesting & thorough report. Apart from the overall view & concentrate now on health as Mr A suggests, is there any pb [illegible] 1 [illegible] can be done [illegible] [illegible] the work of trackers? Probably worth a look. I am attracted by the idea of X, which CST might discuss pre-Budget. [illegible]

c.c. Chief Secretary
Sir P. Middleton
Sir T. Burns
Mr. Kemp
Mr. Odling-Smee
Mr. Spackman
Mr. Turnbull
Mr. Call

LONGER-TERM PUBLIC EXPENDITURE

Mr. Allan's minute of 5th January, enclosing the 1982 Cabinet Papers on longer-term options (which I now return), asked how this now looks, over halfway to 1990.

2. We have done three pieces of work on this.

<u>Economic scenarios</u>

3. First, the report by officials offered two economic scenarios as giving a range of possibilities against which to examine public expenditure trends. Scenario A, with average 2½% GDP growth and 3% productivity between 1980-81 and 1990-91, unemployment falling to 2 million, and 5% inflation in the mid and late 80s, was seen as a somewhat optimistic outcome. Scenario B was more pessimistic, with 1½% productivity, low GDP growth, and inflation and unemployment sticking near their then current levels.

4. The note by Mr. Spackman at flag X compares both scenarios with (in Table 1) how the 1990-91 prospect looks now, and (in Table 2) the 1987-88 outturn. Scenario A is clearly much closer to both the actual and prospective outturns. The main divergences from Scenario A are higher real wages (both public and private) and, consistently with that, higher unemployment; and higher real interest rates.

Expenditure projections

5. Second, the paper by officials contained projections of the main expenditure programmes on both Scenarios. The note by Mr. Turnbull at flag Y calculates the real terms growth expected in these programmes under Scenario A and compares it with the estimated outturn for 1987-88. I had hoped that we might have carried this analysis forward using the 1990 figures from the recent PEWP, but this would have introduced too much bias into the comparison because of the substantial Reserve for 1990-91 in the PEWP. There are also a number of problems in comparing the figures because the content of some programmes has changed; but although this affects the absolute levels of individual programmes, the growth rates can still be compared.

but could have used forecasters'/ exp. groups' best guess as per forecast?

6. The main areas where the 1987-88 figures have turned out higher or lower than the growth rate envisaged in 1982 are:

UP

Social security (mainly due to estimating failure and higher unemployment than in Scenario A)

Education (teacher numbers not falling in line with pupils)

Employment (expanded employment measures)

Home Office/LCD (police pay and more crime)

EC Contributions (raised VAT ceiling)

DOWN

Nationalised Industries (better performance)

Defence (off the NATO hook from 1985-86, and some real decline since then)

CONFIDENTIAL

Housing (higher sales)

Transport (lower subsidies)

DTI (mainly regional)

Other smaller reductions are in IBAP intervention and overseas aid. Health has so far grown just a little slower than in the 1982 projections (though with current pressures this may be reversed by 1990-91).

7. In spite of these differences, the projection of aggregate public expenditure is very close to the mark. Public spending as a percentage of GDP has fallen rather faster than envisaged since 1982-83, due to better GDP growth.

8. The conclusion I draw from this is that we were right not to publish long-term projections for individual programmes in the 1984 Green Paper. They would only have been a hostage to fortune in programmes like defence, while we would still have had to pay for the estimating increase in social security. The same considerations still apply now. But that need not preclude the possibility of issuing an up-dated version of the 1984 Green Paper analysis of total public expenditure and tax, perhaps with the next Autumn Statement or PEWP, if it would help reinforce the argument for continuing prudence with public expenditure in an era of much lower PSBRs.

X

Radical decisions

9. Third, the then Chancellor called for "thorough study and new insights" leading at a later stage to radical decisions affecting most if not all the major programmes. The CPRS paper offered a menu of these. The third paper, by Mr. Kemp, at flag Z, therefore examines where we have got to on these ideas. There is a summary in the first

three pages of the paper. In some cases, of course, Ministers have pursued a different course from that suggested by the CPRS.

10. This is probably the most interesting of the three comparisons. On the whole, I think it represents a reasonable amount of progress at rather more than the half-way mark. We have clearly done better than expected on defence, and some radical decisions (even if of a different kind) are being implemented on education. On social security the cut-back in SERPS and the replacement of single payments by the Social Fund are both advances; my own view is that the CPRS idea (of getting off the RPI indexation and leaving each uprating to be done on its merits) would quite as likely have resulted in more expenditure rather than less.

I agree

11. Some substantial advances have also been made on housing and regional policy. Privatisation has been pressed forward, and the nationalised industries made more profitable. The new system of local government finance will place the cost of marginal spending decisions more squarely on the local chargepayer; and a new planning total, excluding locally-financed local spending, is on the way to being implemented. EC contributions, as one might have expected, are an area of continuing struggle, but Fontainebleau has substantially reduced the budgetary burden below what it would otherwise have been.

12. The obvious conclusion to draw from this part of the analysis is the need to review health, and that is in hand.

J. ANSON

LONGER-TERM PUBLIC EXPENDITURE: ECONOMIC SCENARIOS

Two economic scenarios were used in the 1982 exercise. The 1982 report said that scenario A "implies an all round improvement in our affairs and may not be far short of the best we can expect". Scenario B reflected "much less favourable economic assumptions", and was not seen at the time as being more or less likely than scenario A. It was said that the two scenarios "seemed to cover an adequate range of possibilities".

3. The two attached tables show where the economy is in relation to these scenarios. Table 1 shows the latest projections for the whole period up to 1990-91 on the basis of the January forecast up to 1989 and a preliminary version of the 1988 MTFS projections beyond that. Table 2 shows actual progress up to the forecast outcome in 1987-88. In both tables the growth rates are measured from 1980-81 as in the original exercise, although the expenditure projections were measured from 1982-83. In scenario A output growth from 1982-83 was faster than from 1980-81 because of the slow growth up to 1982-83.

4. For output and productivity growth and inflation, the outturn has generally been very close to scenario A. However real wages have grown more rapidly than in scenario A and unemployment is higher. Real interest rates are also much higher than in either scenario.

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Table 1

(Average annual growth rates from 1980-81 to 1990-91 unless otherwise stated)

	SCENARIO A	**SCENARIO B**	**LATEST PROJECTIONS**(1)
GDP(A)	$2\frac{1}{2}$%	$\frac{3}{4}$% 1980-81 to 1985-86 $\frac{1}{2}$% 1985-86 to 1990-91	$2\frac{3}{4}$%
Productivity (whole economy excluding public non-trading)	3%	$1\frac{1}{2}$%	3%
Unemployment (narrow definition, millions, 1990-91)	2	3	2.4(2)
Inflation (GDP deflator)	5% in mid and late 1980s	10% in mid and late 1980s	5% in mid-1980s, declining to $3\frac{1}{2}$% by 1990-91
Real interest rate (1990-91)**(3)**	2%	2%	6% (2)
Real effective exchange rate (1980=100, 1990-91)	83	83	86(2)
Real wages(4):			
private sector	$1\frac{1}{2}$%	$1\frac{1}{2}$%	$2\frac{1}{2}$%
public non-trading sector	$\frac{1}{2}$%	$\frac{1}{4}$%	$1\frac{3}{4}$%

(1) Outturns to 1987, January forecast to 1989 and a preliminary version of 1988 MTFS projections beyond that

(2) The estimated outturns in 1987-88 are:

unemployment	2.75
real interest rate	6%
real effective exchange rate	82

(3) Short-term nominal rate minus rate of increase of consumers' expenditure deflator

(4) Deflated by GDP deflator.

Table 2

(Average annual growth rates from 1980-81 to 1987-88 unless otherwise stated)

	SCENARIO A	**SCENARIO B**	**ESTIMATED OUTTURN (January forecast)**
GDP(A)	2½%	¾%	2¾%
Productivity (whole economy excluding public non-trading)	3%	1½%	3¼%
Inflation (GDP deflator)	5% (in mid and late 80s)	10% (in mid and late 80s)	4½% (average for 3 yrs to 1987-88) 5% (in 1987-88)
Real wages(1)**:**			
private sector	1½%	1½%	2½%
public non-trading sector	½%	¼%	1%

(1) Deflated by GDP deflator

Note: The values in 1987-88 of those variables which were given only 1990-91 values in the 1982 scenarios, with no presumed path through the intervening years, are shown in footnote (2) of Table 1. The variables are unemployment, interest rates and the exchange rate.

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LONG-TERM PUBLIC EXPENDITURE

Introduction

This note compares the development of individual programmes between 1982-83 and 1987-88 with that envisaged in the LTPE report of 1982. The latter showed for each programme an estimated growth between 1982-83 and 1990-91 in cost (what we now call real) terms, for two scenarios, A and B. Under A growth was assumed to be 2½ per cent a year with unemployment getting down to 2 million by 1990-91; under B growth was ½ per cent a year with unemployment at 3 million. As the economy has grown somewhat faster even than scenario A the comparisons of outturn are made with the scenario A figures.

The Programmes

2. Table 1 calculates the amount by which expenditure on individual programmes was higher or lower than if they had grown in line with the LTPE projections. Col 1 takes the real terms growth for each programme projected over eight years and converts it into "Par", ie the increase that would have been expected with a constant growth over the first five of the eight years, ie to 1987-88. Col 2 shows the change which actually took place over the first five years. Although the precise coverage of some of the programmes has changed, the growth rates of the programmes as now defined are comparable. Col 3 shows, in 1987-88 prices, how much more or less would be spent on the programme if the change had been exactly at par.

3. The following differences emerge:

(i) Defence. **Saving: £1.8 billion.** LTPE assumed 3 per cent growth continuing to 1988-89. In practice it was ended in 1985-86 since when there has been some real decline. (Calculation based on the zero RPE case.)

(ii) FCO/Aid. **Saving: £0.3 billion.** LTPE assumed the aid programme would rise from 0.4 per cent of GDP to 0.5 per cent. It has fallen to 0.3 per cent.

in line with demographic trends.

(xii) Health and Personal Social Services. **Saving: £0.2 billion.** Given size of programme a remarkably accurate projection with real spending rising at 2½ per cent a year against LTPE projection of 2¾ per cent. (But it seems likely, in the face of current pressures, that growth will accelerate and by 1990-91 will exceed the LTPE projection.)

(xiii) Social Security. **Excess: £4.2 billion.** The error of 10 per cent on the level represents about 2 per cent a year on the growth rate. In part a reflection of smaller fall in unemployment than assumed, but principally failure to estimate the underlying growth in benefit payments. However, disentangling the two is not straightforward as what was recorded as underlying growth may have been a delayed reaction to the rise in unemployment, eg a tendency for long-term unemployed to switch to sickness and disablement benefits. It is likely also that the 1982-83 plans which LTPE used as the starting point for the exercise were an underestimate.

(xix) Nationalised Industries. **Saving £1.9 billion.** The biggest changes were in Steel (from £569 million to -£300 million) and Electricity (England & Wales) (-£154 million to -£1,164 million), National Bus (+£62 million to -£127 million) and water (£291 milliion to £25 million).

The aggregates

4. LTPE used the concept of the planning total plus net debt interest rather than GGE. Table 2 shows that, under scenario A, total public spending so defined was projected to grow by 1.45 per cent per annum. Despite the very large errors on individual programmes, the projection for the aggregate proved extremely accurate. In the five years to 1987-88 the average growth was 1.55 per cent per annum.

5. As a proportion of GDP, total public spending was projected to fall, over the eight years to 1990-91, from 44.2 per cent to 39.3 per cent, a drop of 4.9 percentage points. In the five years to 1987-88, using current estimates of GDP, it fell from

(iii) EC contributions. **Excess: £0.6 billion.** Maintenance of the 1 per cent VAT ceiling was assumed.

EC contributions

(iv) IBAP. **Saving £0.4 billion.** Big increases in intervention were assumed. In practice the projection is better than it looks as the 1987-88 outturn is flattered by fortunate exports from the 1986 harvest and a very small yield from the 1987 harvest.

(v) Employment. **Excess: £0.9 billion.** Reflects greater expansion of employment and training measures. Despite this, unemployment (narrow definition) has averaged 2.7 million in 1987-88, against the 2.45 million it would have been at if progressing steadily from 2.75 million in 1982-83 to 2 million in 1990-91.

(vi) DTI/ECGD/Energy. **Saving: £0.8 billion.** Principally reflects assumption that regional spending would remain at existing level.

(vii) Transport. **Saving: £1.2 billion.** Principally reflects faster progress on reducing local authority public transport subsidies. (Figure may be flattered by inclusion of LRT in base year but not in final year.)

(viii) Housing. **Saving: £1.3 billion.** LTPE assumed receipts had reached their peak. In practice they were 7 per cent higher in real terms in 1987-88 than in 1982-83.

(ix) OES. **Saving nil.** Higher local authority and new towns receipts have offset higher local authority current expenditure and urban programme and UDCs.

(x) DES/OAL. **Excess: £1.6 billion.** LTPE assumed teacher numbers would fall in line with pupil numbers, keeping real expenditure per pupil constant. Reduction in pupil/teacher ratio plus higher real pay produced substantial increase.

(xi) Home Office/Legal Depts. **Excess: £0.7 billion.** Principally indexed police pay and failure of growth in crime to moderate

43.2 per cent to 39.4 per cent, a drop of 3.8 percentage points. This is a steeper trend than envisaged. With expenditure in real terms growing more or less on track, the difference lies in the growth of GDP. Between 1982-83 and 1990-91, an annual rate of 2.9 per cent was projected (consistent with the 2½ per cent starting in 1980-81 assumed in scenario A). But over the five years to 1987-88, a rate of 3.4 per cent was achieved (consistent with the 2¾ per cent from 1980-81).

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COMPARISON OF LTPE PROJECTIONS WITH 1987-88 OUTTURN[1]

Table 1

Department	PAR	Actual	Saving-/Excess+
	Percentage change, real terms 1982-83 to 1987-88		£ billion
Defence	15.6	5.6	-1790
FCO	27.9	10.3	-325
EC Contributions	12.4	91.1	+575
MAFF	-6.3	-9.9	-28
IBAP	27.4	-3.1	-400
Employment	2.9	33.0	+895
DTI/ECGD/Energy	-4.8	-32.3	-773
Transport	18.8	-10.4	-1270
Housing	12.6	-27.3	-1343
OES	-2.4	-3.4	-39
DES/OAL	-1.2	8.8	+1650
HO/Legal Depts	11.5	28.7	+709
HPSS	14.6	13.4	-201
SS	4.4	15.0	+4242
Nat Ind	-12.0	-82.9	-1882
Total above programmes			+20

EC contributions

[1] Outturn as in 1988 PEWP

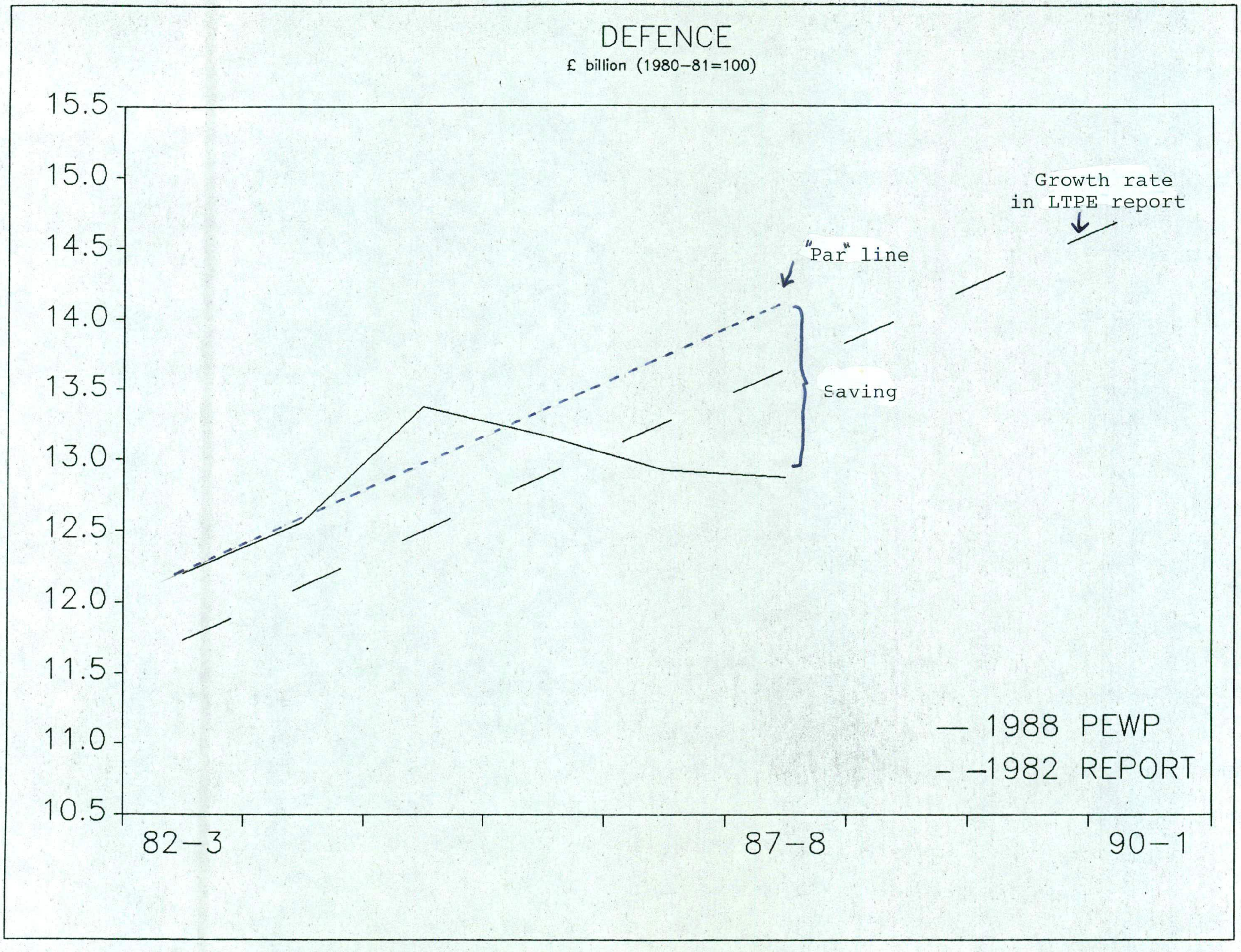
Table 2

	LTPE 1982-83 to 1990-91	Actual 1982-83 to 1987-88
	Annual or percentage change	
Planning total + net debt interest - priv proceeds	1.45	1.53
Money GDP	2.9	3.4
Public Spending / GDP	44.2 to 39.3	43.2 to 39.4

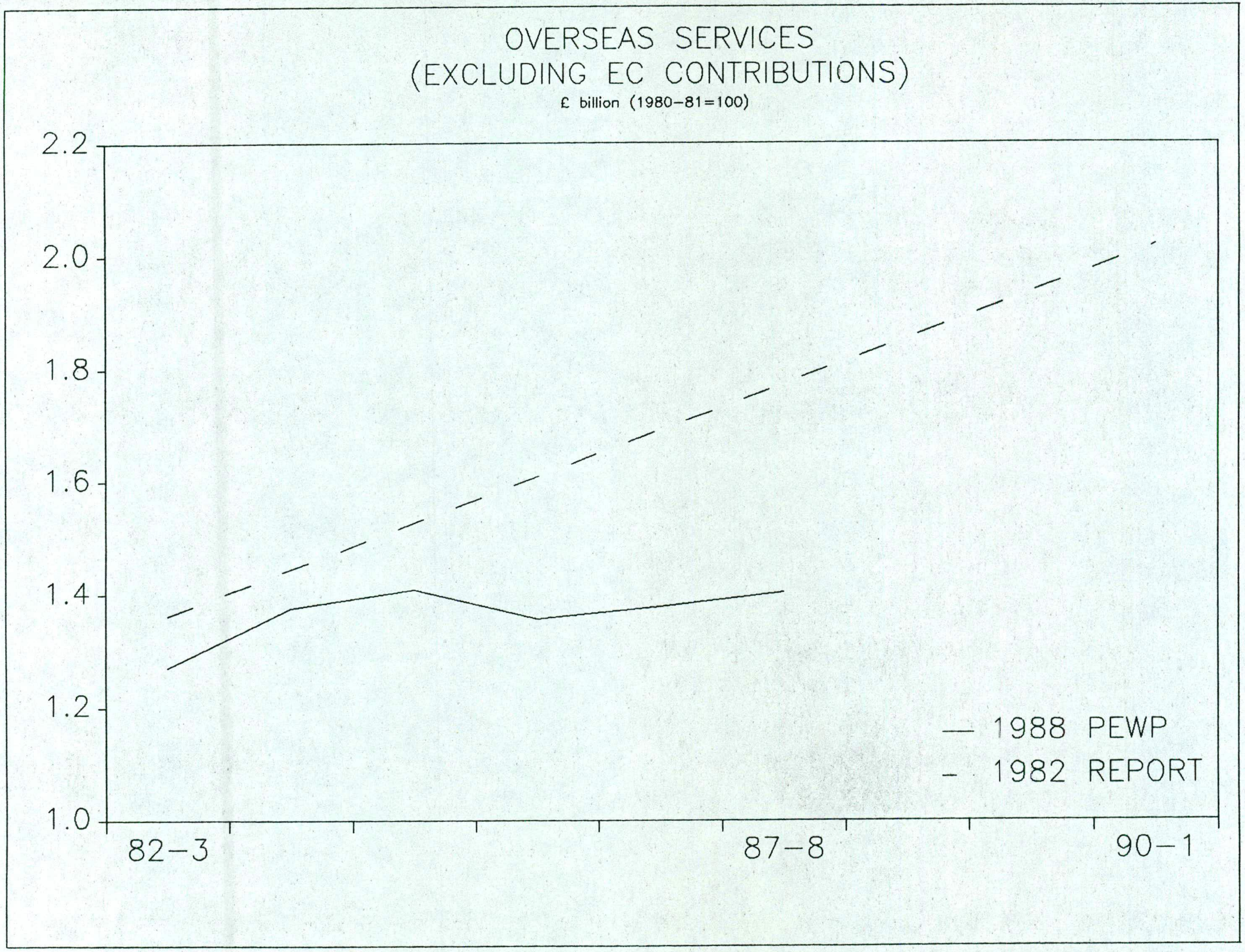
NOTES TO THE CHARTS

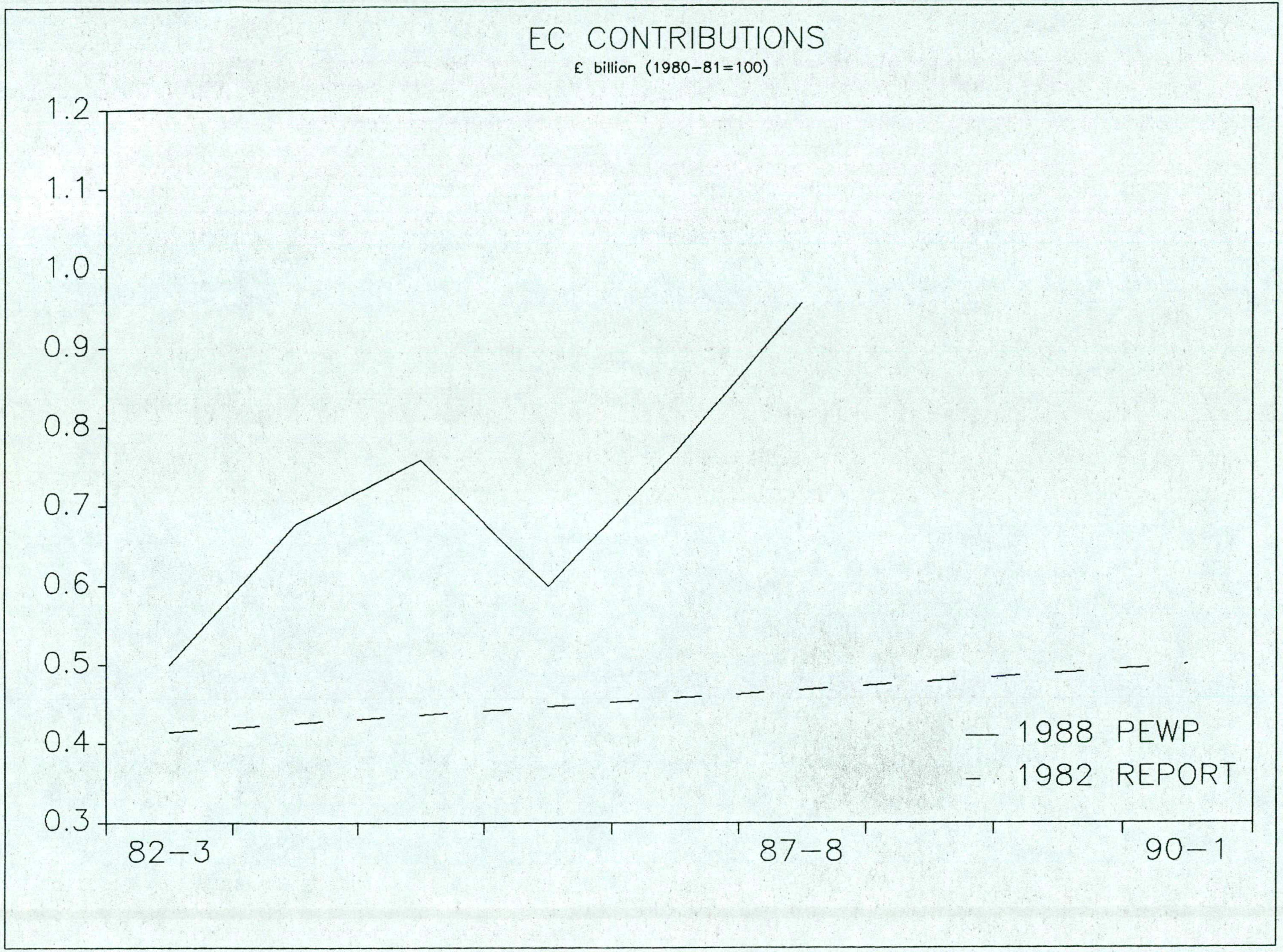
(i) In the attached charts, the "saving" or "excess" calculated in Table 1 can be illustrated by comparing the position actually reached in 1987-88 with the position that would have been reached had spending started at the actual 1982-83 level and then moved along on a growth line parallel to that in the LTPE report. The resulting gap is then converted into 1987-88 prices. This is set out in the defence chart.

(ii) The actual level recorded for a programme in 1982-83 can differ from the figure used in the LTPE report. This difference in the starting point can arise because of subsequent classification changes or because the outturn in 1982-83 was different from that in the plans as seen in June 1982 when the report was produced.

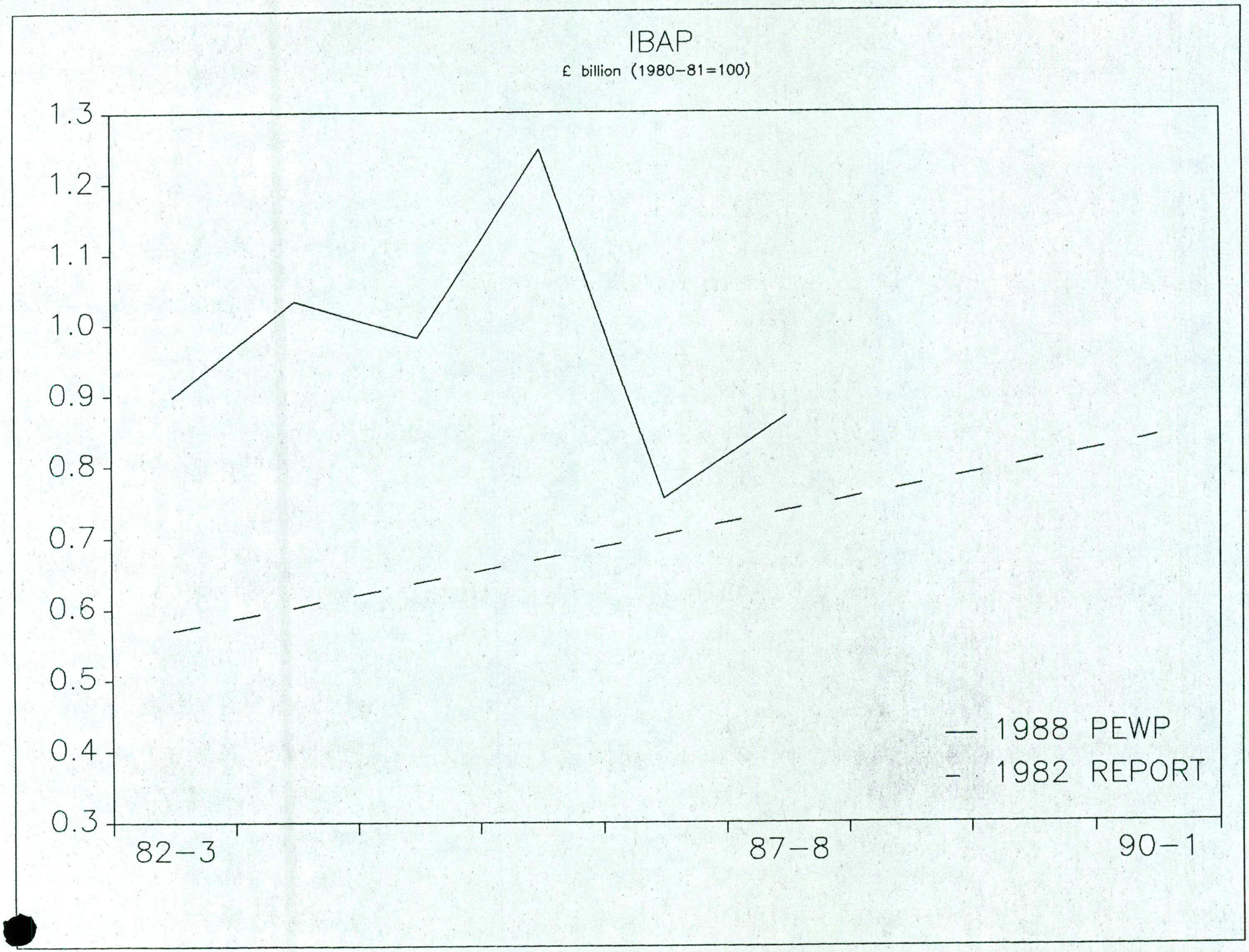


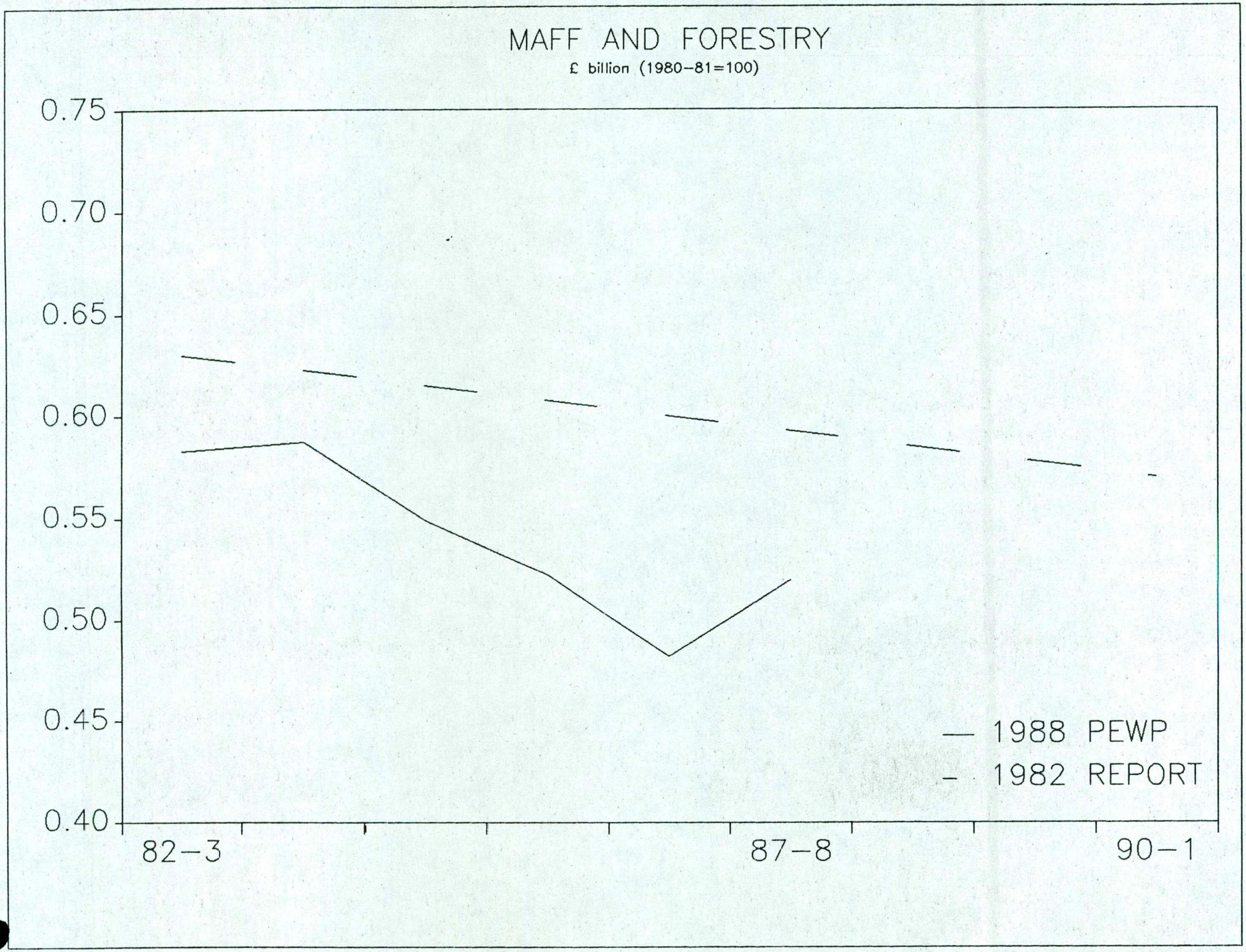
DEFENCE
£ billion (1980-81=100)
15.5
15.0
14.5
14.0
13.5
13.0
12.5
12.0
11.5
11.0
10.5
82-3
87-8
90-1
Growth rate in LTPE report
"Par" line
Saving
1988 PEWP
1982 REPORT


OVERSEAS SERVICES
(EXCLUDING EC CONTRIBUTIONS)
£ billion (1980-81=100)
2.2
2.0
1.8
1.6
1.4
1.2
1.0
82-3
87-8
90-1
1988 PEWP
1982 REPORT

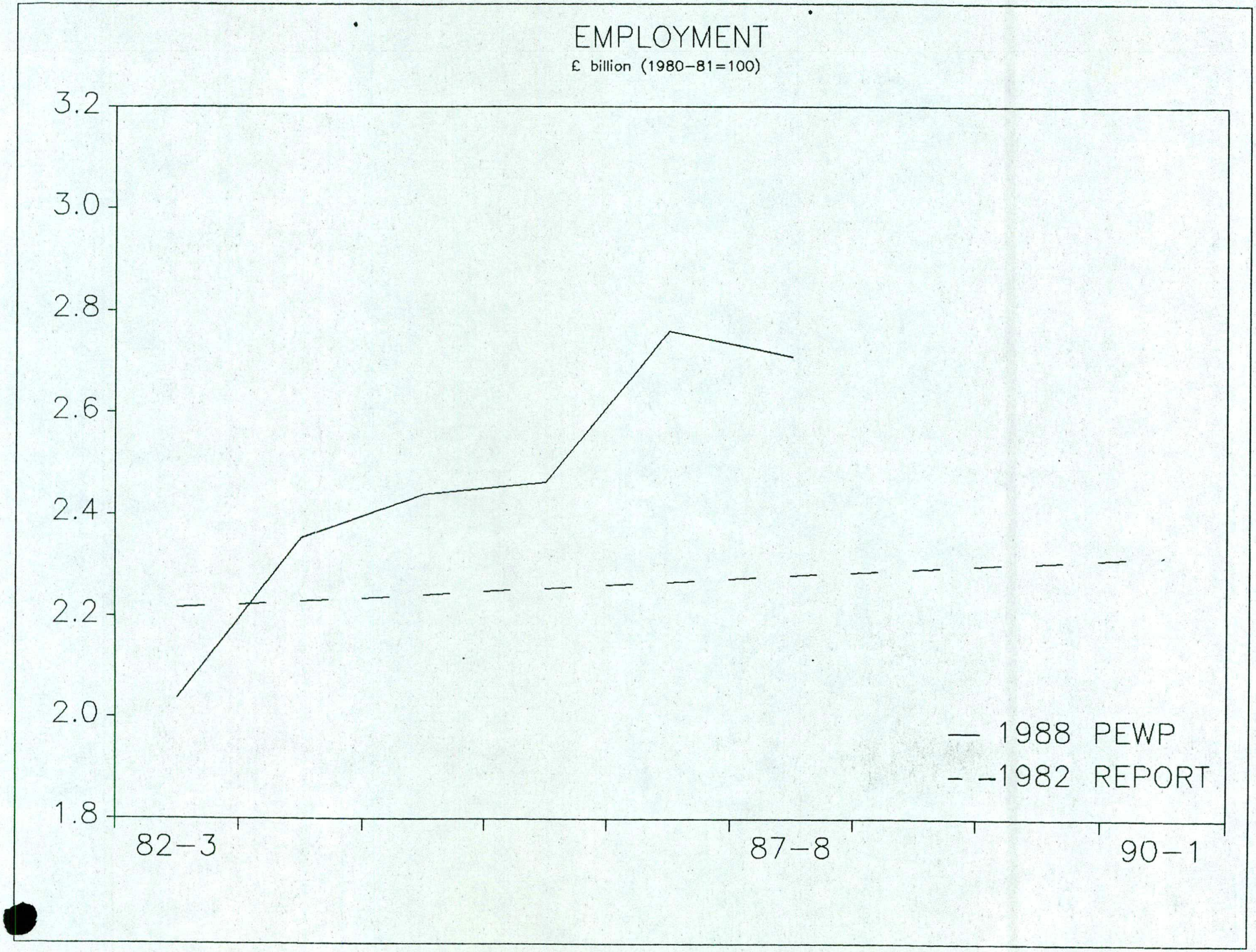


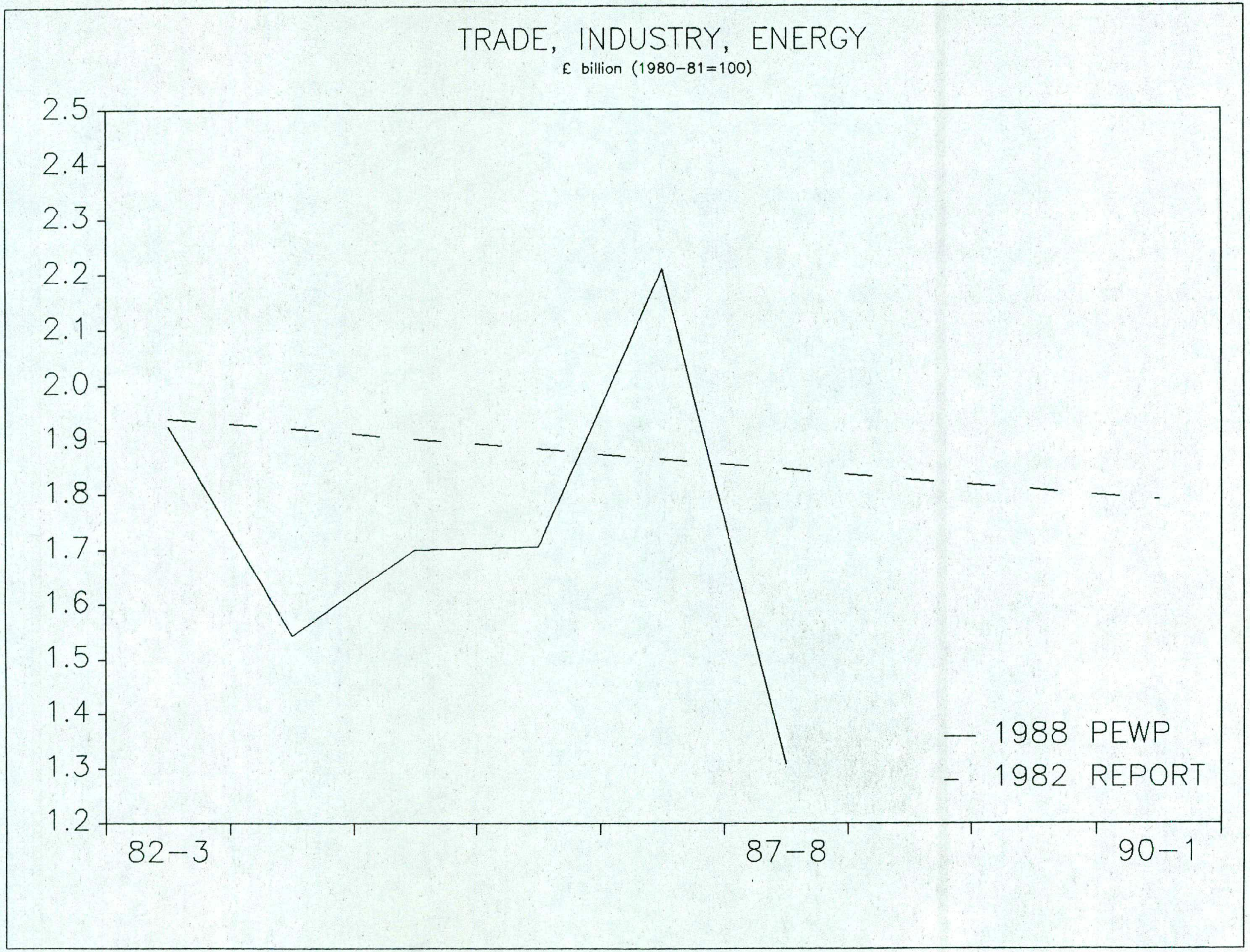
EC contributions

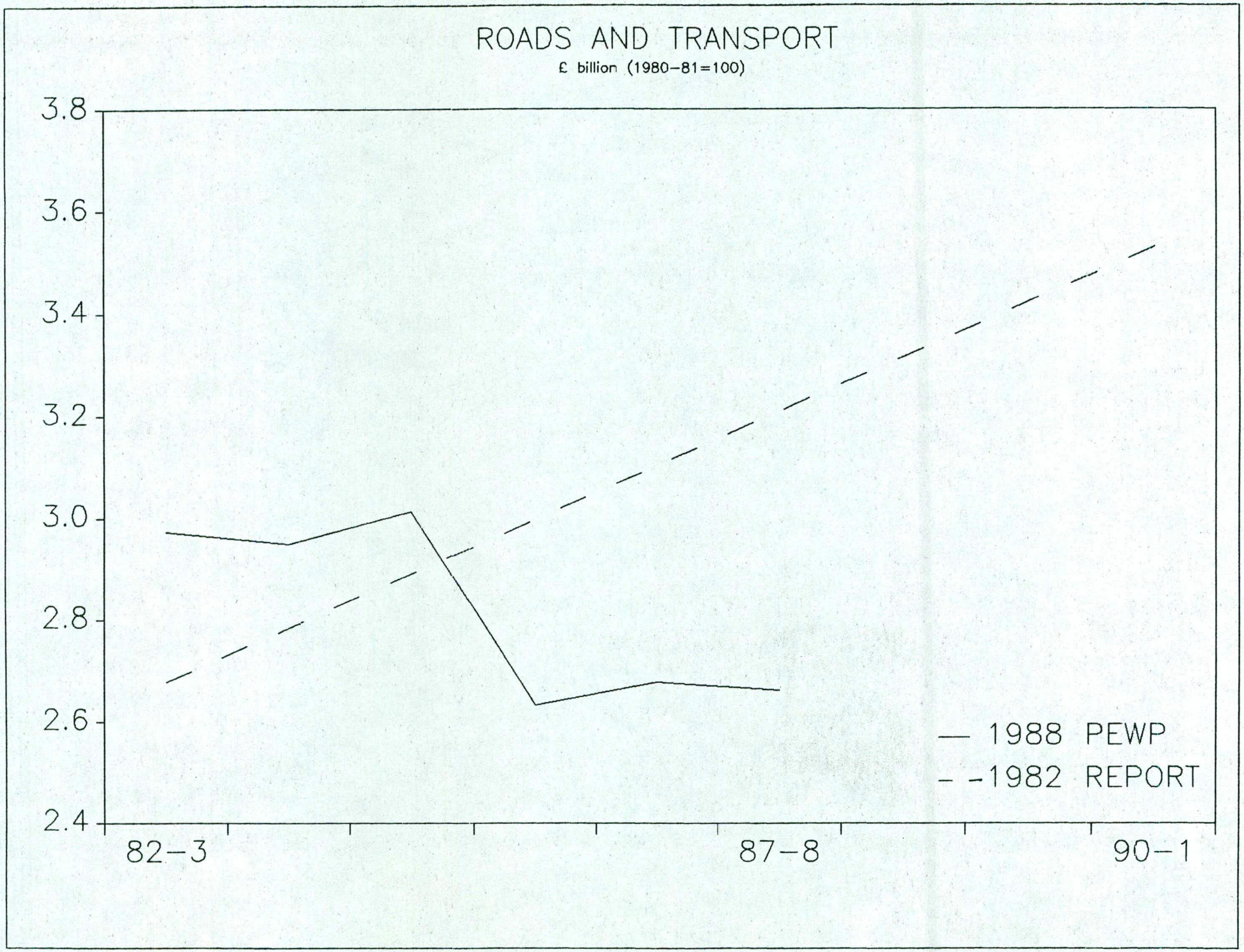

IBAP
£ billion (1980-81=100)
1.3
1.2
1.1
1.0
0.9
0.8
0.7
0.6
0.5
0.4
0.3
82-3
87-8
90-1
— 1988 PEWP
– 1982 REPORT

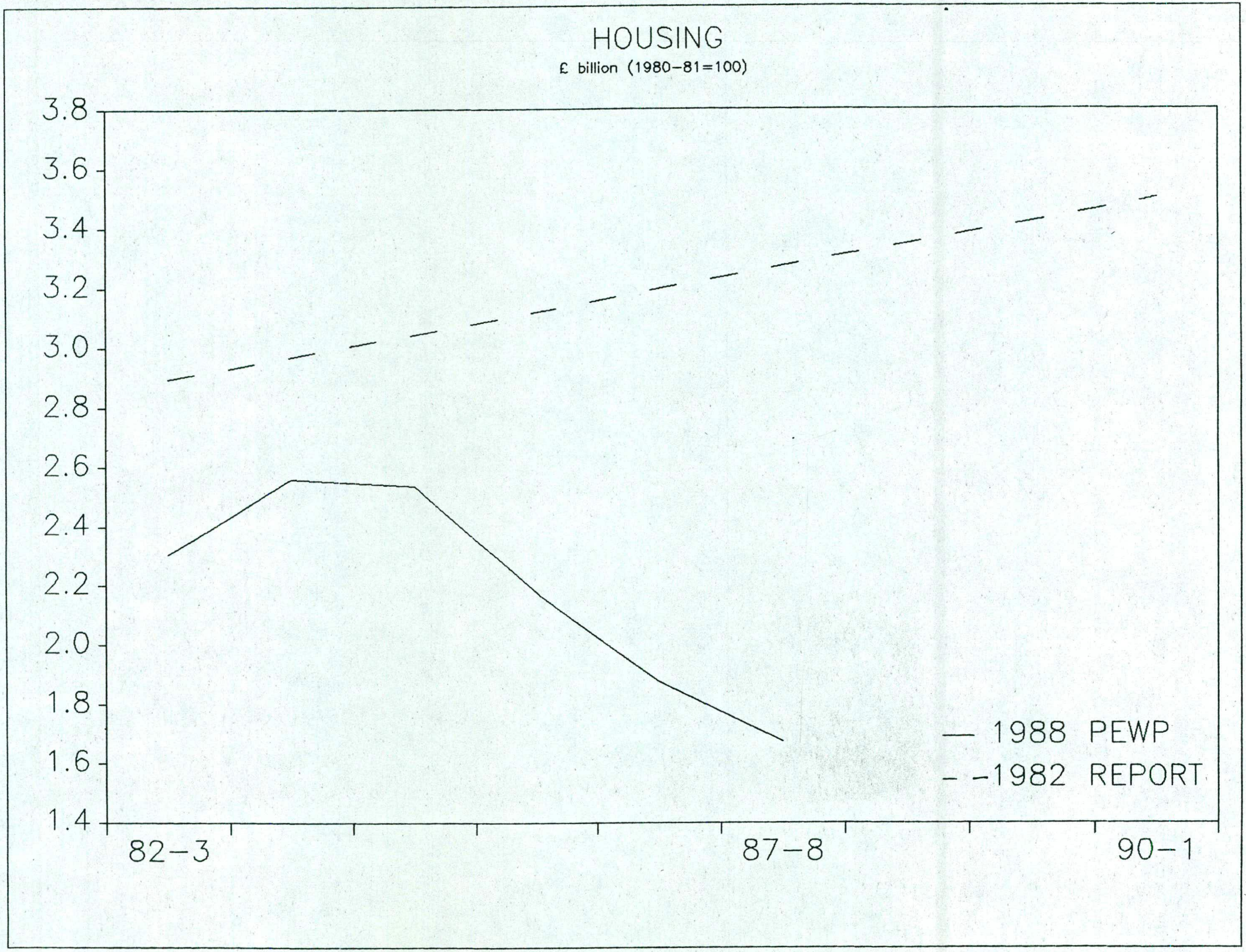


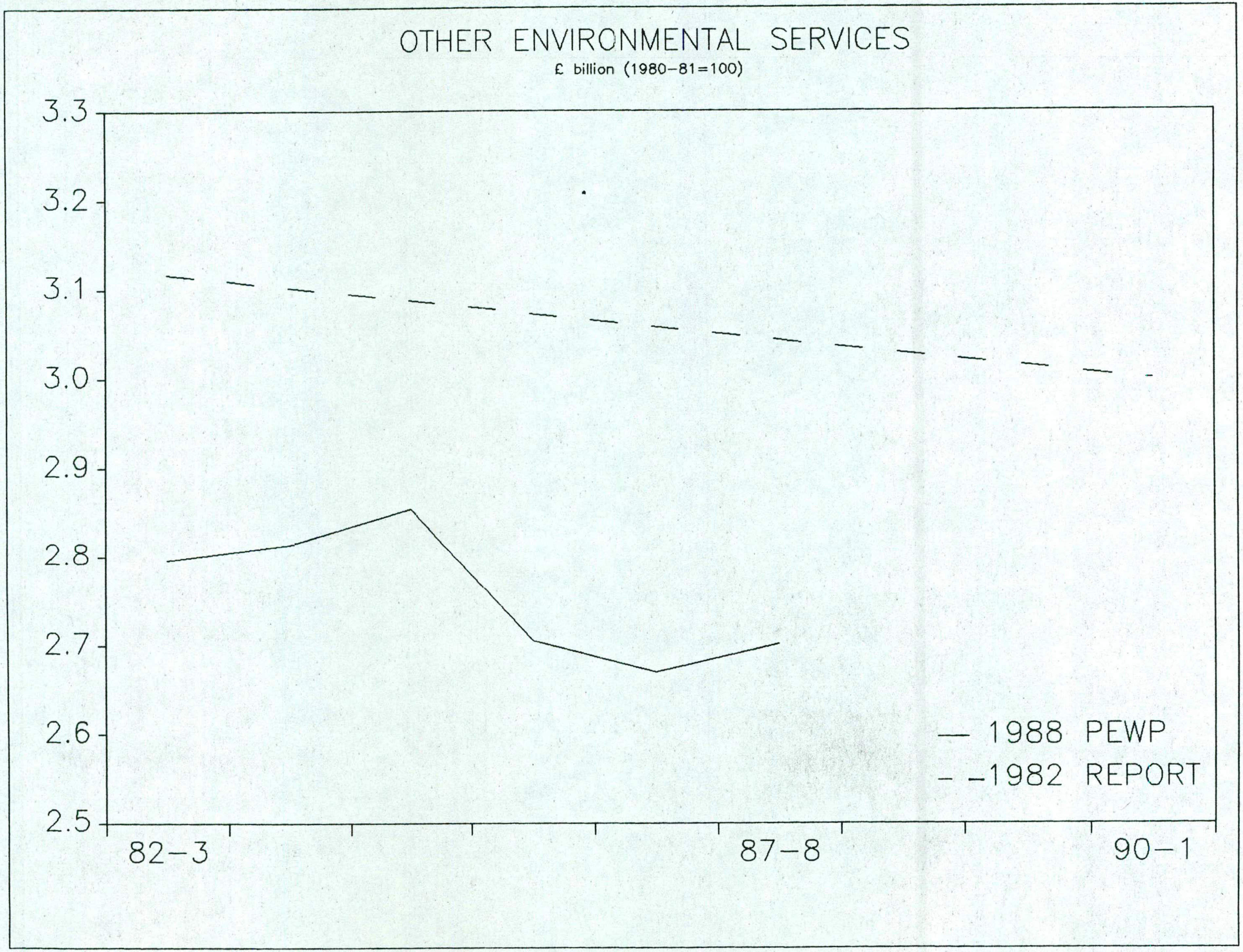
MAFF AND FORESTRY
£ billion (1980-81=100)
0.75
0.70
0.65
0.60
0.55
0.50
0.45
0.40
82-3
87-8
90-1
— 1988 PEWP
- 1982 REPORT


EMPLOYMENT
£ billion (1980-81=100)
3.2
3.0
2.8
2.6
2.4
2.2
2.0
1.8
82-3
87-8
90-1
— 1988 PEWP
- -1982 REPORT

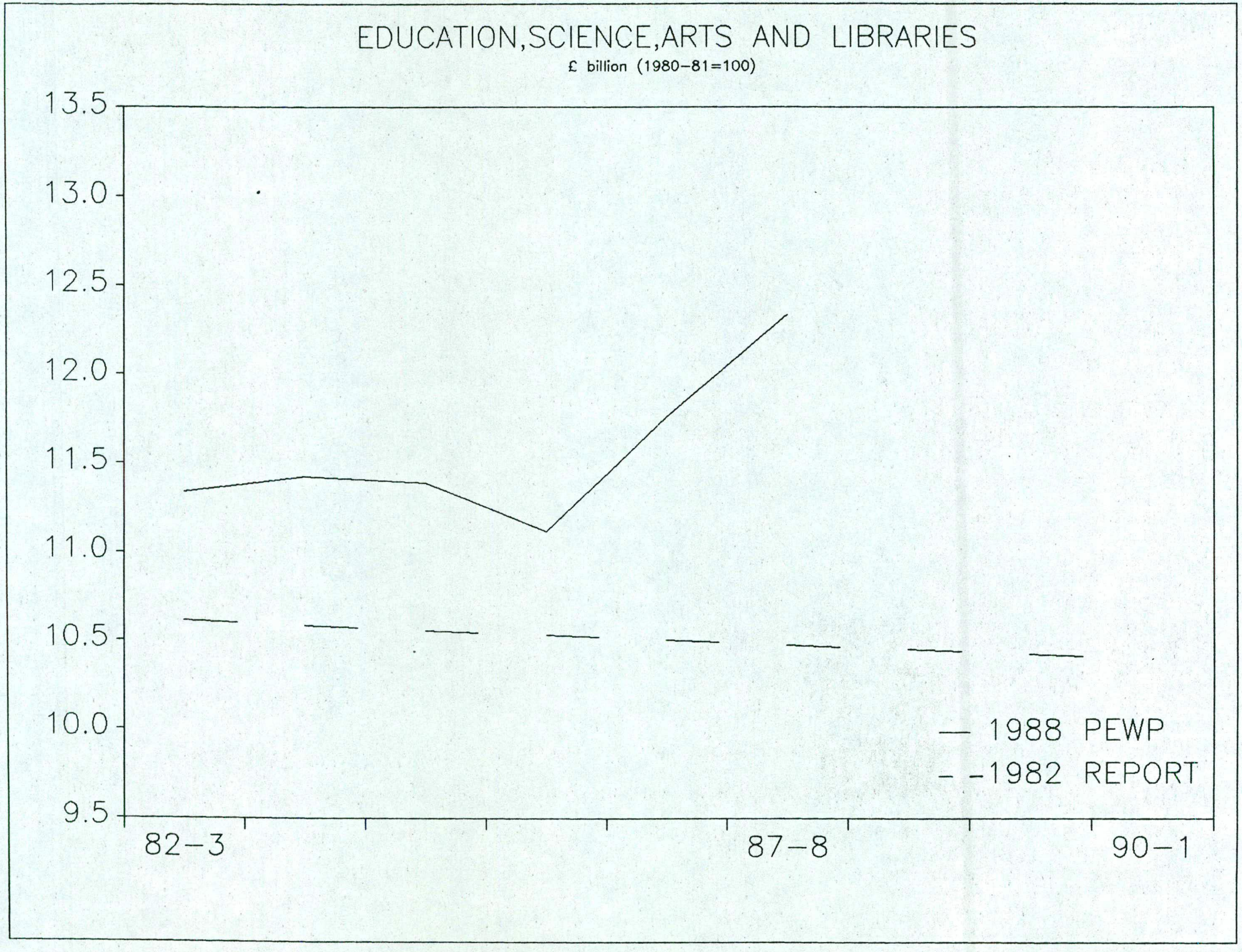

TRADE, INDUSTRY, ENERGY
£ billion (1980-81=100)
2.5
2.4
2.3
2.2
2.1
2.0
1.9
1.8
1.7
1.6
1.5
1.4
1.3
1.2
82-3
87-8
90-1
— 1988 PEWP
- 1982 REPORT

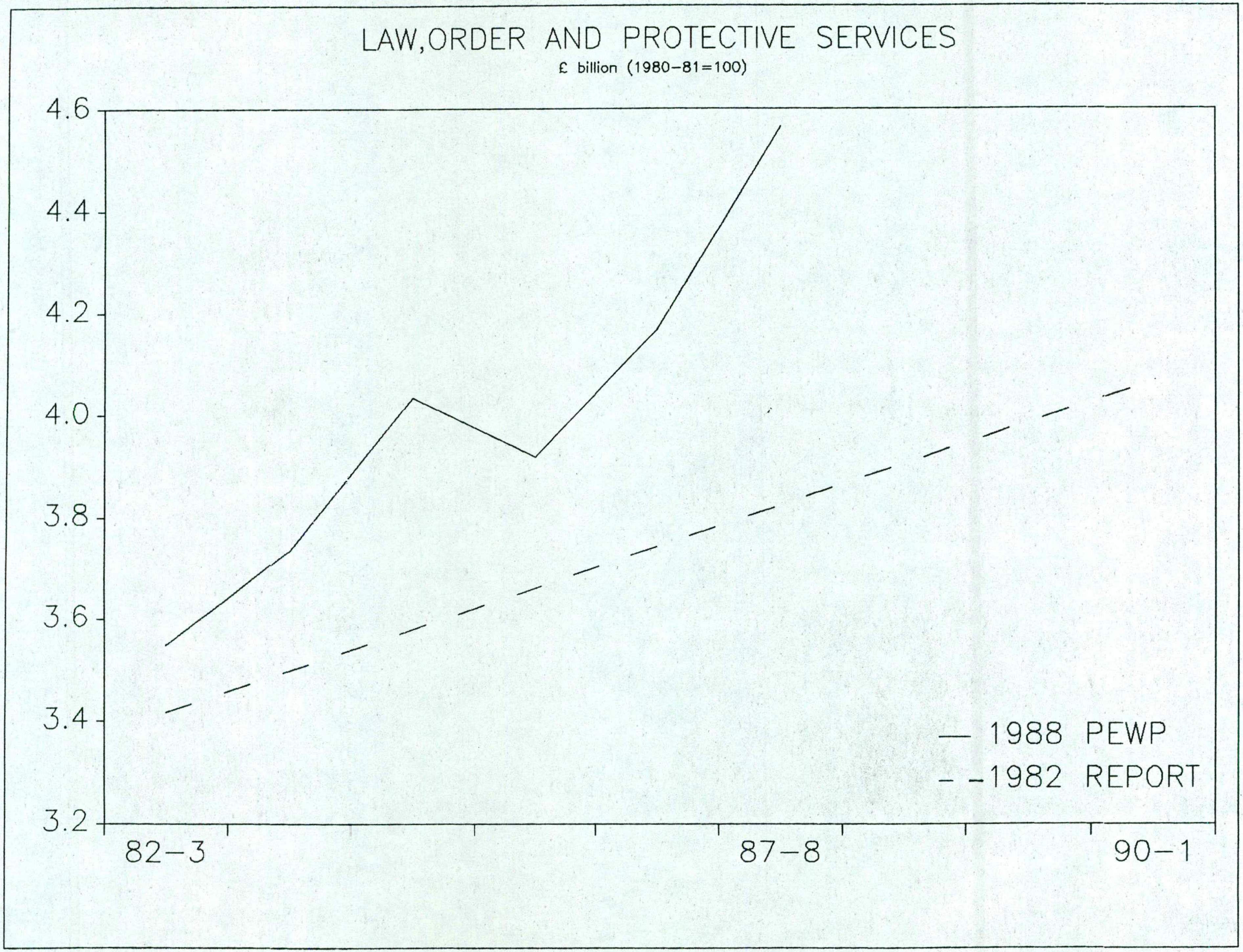

ROADS AND TRANSPORT
£ billion (1980-81=100)
3.8
3.6
3.4
3.2
3.0
2.8
2.6
2.4
82-3
87-8
90-1
— 1988 PEWP
- -1982 REPORT

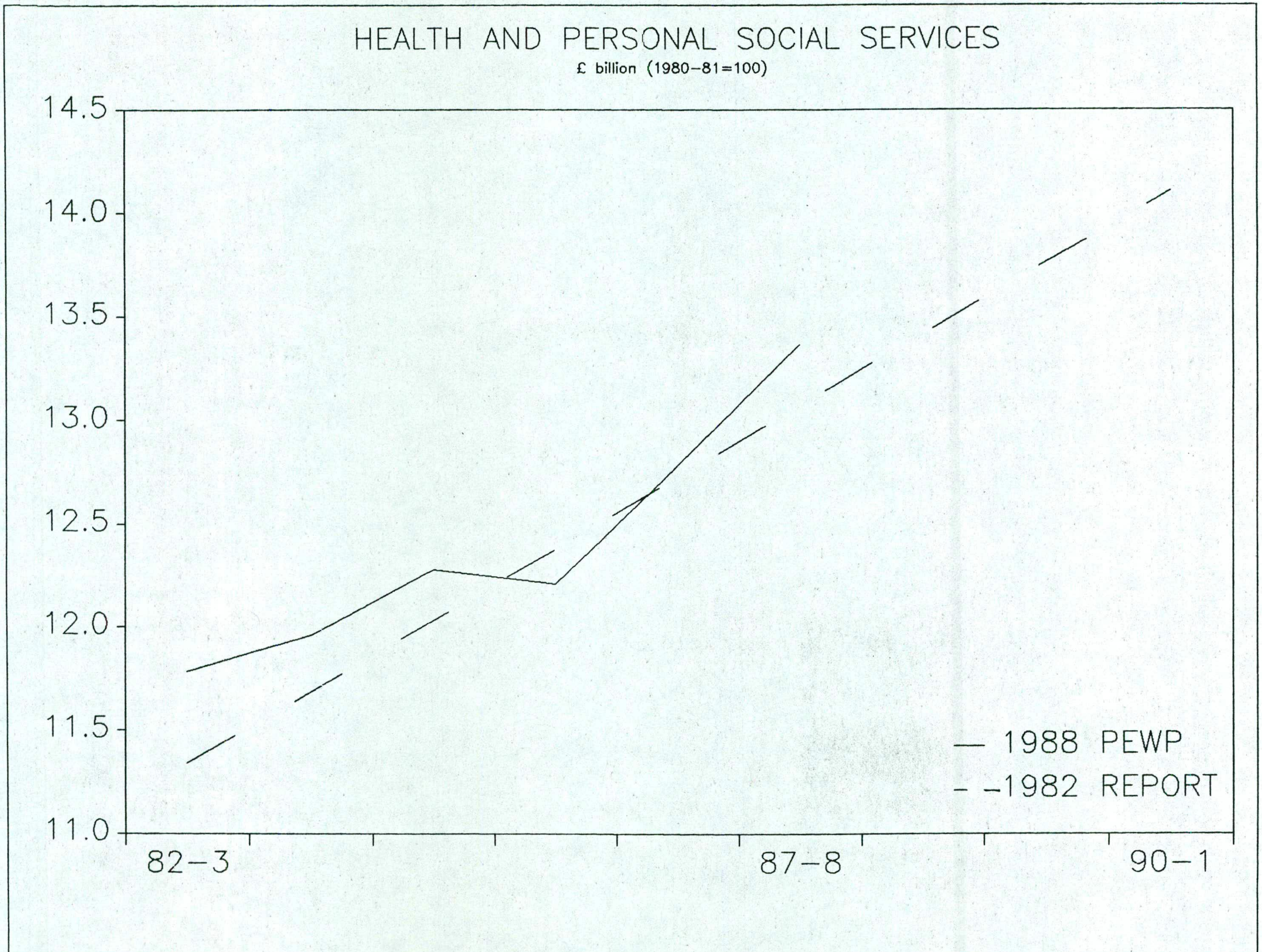

HOUSING
£ billion (1980-81=100)
3.8
3.6
3.4
3.2
3.0
2.8
2.6
2.4
2.2
2.0
1.8
1.6
1.4
82-3
87-8
90-1
— 1988 PEWP
- -1982 REPORT

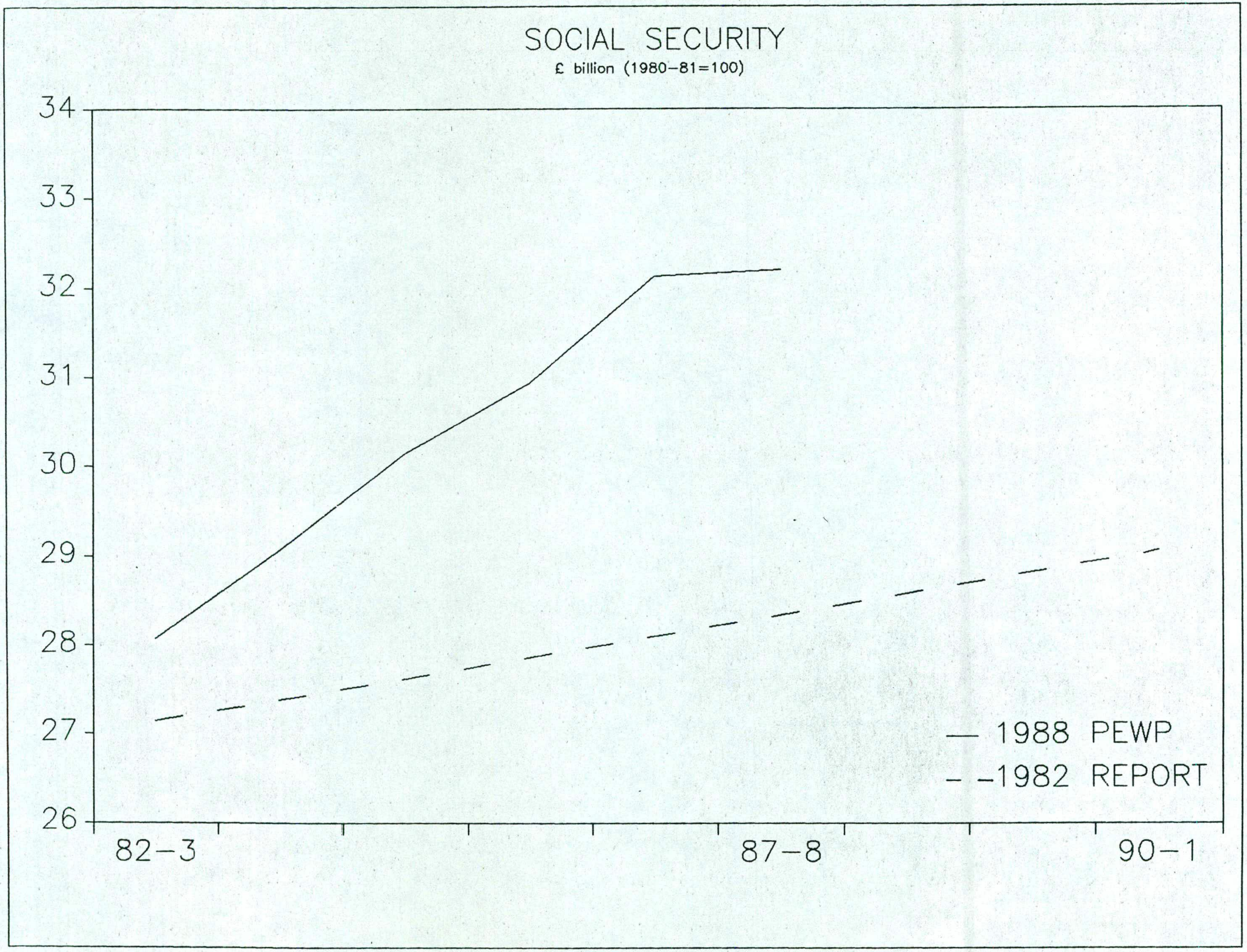


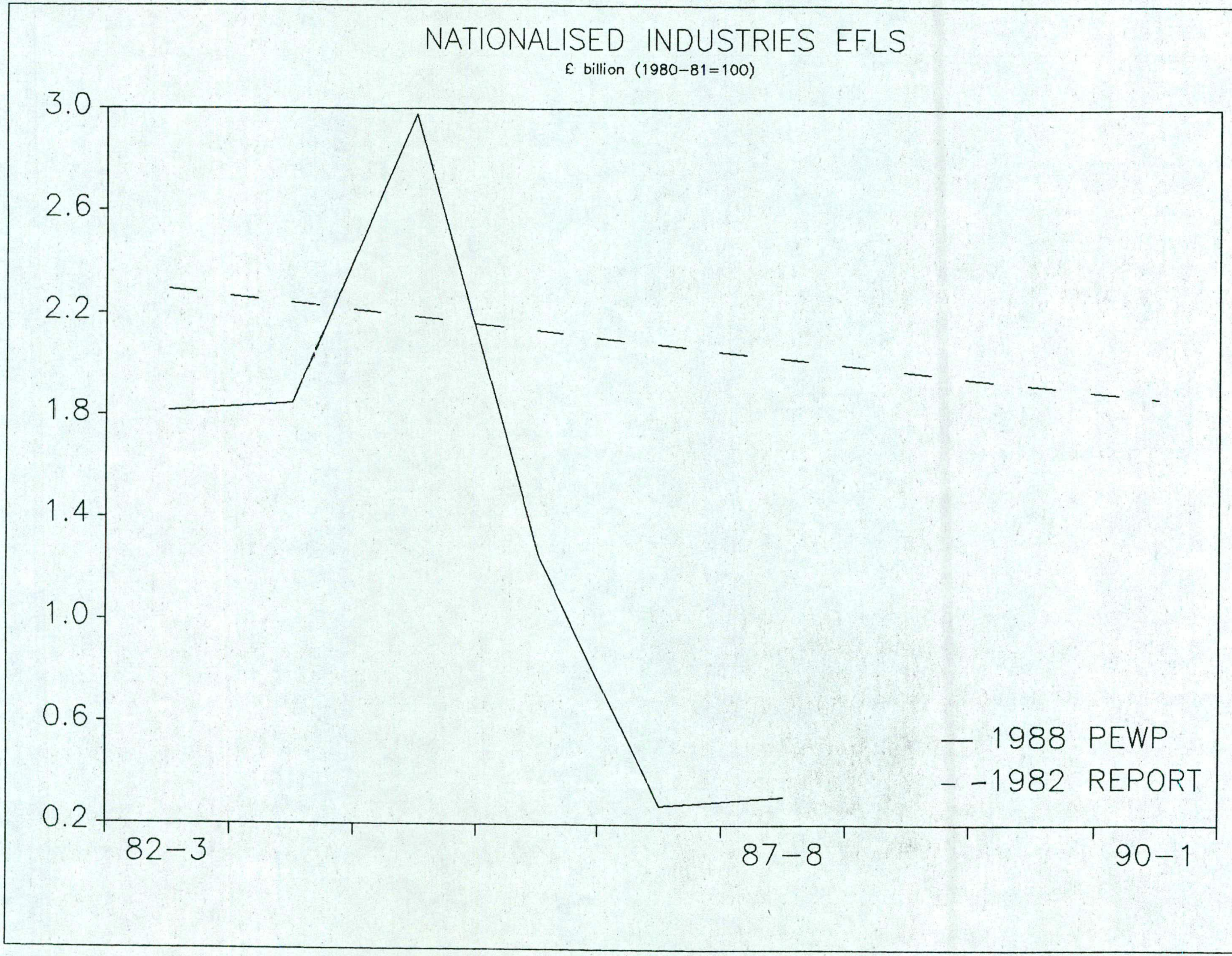
OTHER ENVIRONMENTAL SERVICES
£ billion (1980-81=100)
3.3
3.2
3.1
3.0
2.9
2.8
2.7
2.6
2.5
82-3
87-8
90-1
— 1988 PEWP
- -1982 REPORT


EDUCATION,SCIENCE,ARTS AND LIBRARIES
£ billion (1980-81=100)
13.5
13.0
12.5
12.0
11.5
11.0
10.5
10.0
9.5
82-3
87-8
90-1
— 1988 PEWP
- -1982 REPORT

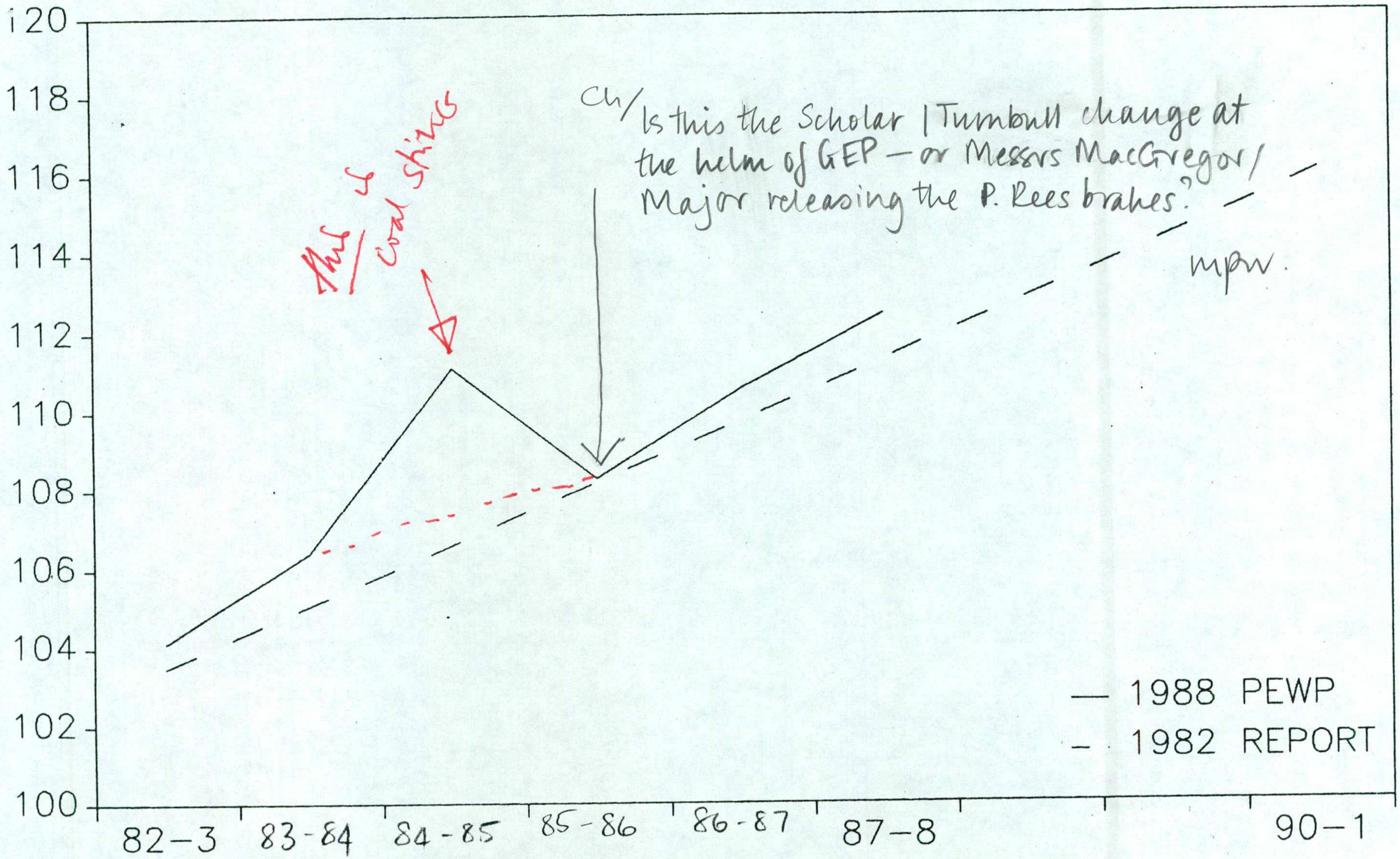

LAW,ORDER AND PROTECTIVE SERVICES
£ billion (1980-81=100)
4.6
4.4
4.2
4.0
3.8
3.6
3.4
3.2
82-3
87-8
90-1
— 1988 PEWP
- -1982 REPORT


HEALTH AND PERSONAL SOCIAL SERVICES
£ billion (1980-81=100)
14.5
14.0
13.5
13.0
12.5
12.0
11.5
11.0
82-3
87-8
90-1
1988 PEWP
1982 REPORT


SOCIAL SECURITY
£ billion (1980-81=100)
34
33
32
31
30
29
28
27
26
82-3
87-8
90-1
— 1988 PEWP
- -1982 REPORT


NATIONALISED INDUSTRIES EFLS
£ billion (1980-81=100)
3.0
2.6
2.2
1.8
1.4
1.0
0.6
0.2
82-3
87-8
90-1
1988 PEWP
-1982 REPORT

PLANNING TOTAL
(including net debt interest exc pp)
£ billion (1980-81=100)



TERM PUBLIC EXPENDITURE- Figures used in 1982 Report.

	£million (1980-81=100)			Percentage of GDP	
	1982-83	1990-91	Percentage change	1982-83	1990-91
PROGRAMME (1)					
Defence	11,732	14,800	26.2	5.0	5.0
Aid + other overseas serv.	1,363	2,020	48.2	0.6	0.7
FCO Diplomatic					
EC Contributions	415	500	20.5	0.2	0.2
Overseas services (2)	1,778	2,520	41.7	0.8	0.9
MAFF	577	520	-9.9	0.2	0.2
IBAP	570	840	47.4	0.2	0.3
Forestry	53	50	-5.7	-	-
Agriculture,fisheries,food and forestry (2)	1,200	1,410	17.5	0.5	0.5
Employment	2,216	2,320	4.7	0.9	0.8
DTI/ECGD/Energy	1,935	1,790	-7.5	na	na
Trade,Industry,energy and employment (2)	4,151	4,110	-1.0	1.8	1.2
Roads and Transport	2,678	3,530	31.8	1.2	1.2
Housing	2,895	3,500	20.9	1.2	1.2
Other environmental services	3,117	3,000	-3.8	1.3	1.0
Education and Science and Arts and Libraries	10,610	10,400	-2.0	4.5	3.5
Law,order and protective services	3,417	4,070	19.1	1.5	1.4
Health and personal social services (2)	11,341	14,110	24.4	4.8	4.8
Social security	26,646	28,560	7.2	11.3	9.7
Nationalised industries EFLs	2,293	1,870	-18.4	1.0	0.6
Other dept. programmes (3)	12,507	13,520	8.1	na	na
Planning total + net debt interest + priv proceeds	103,400	116,000	12.2	44.2	39.3

(1) Excluding Nationalised Industries EFLs.
(2) Sum of previous components.
(3) Includes Wales, Scotland and Northern Ireland.

EC Contributions

[illegible] TERM PUBLIC EXPENDITURE - consistent with 1988 PEWP

	£million (1980-81=100)			Percentage of GDP	
	1982-83	1987-88	Percentage change	1982-83	1987-88
PROGRAMME (1)					
Defence	12,199	12,878	5.6	5.1	4.5
Aid	862	921	6.9	0.4	0.3
FCO Diplomatic	404	475	17.5	0.2	0.2
EC Contributions	500	956	91.1	0.2	0.3
Other	6	8	26.8	0.0	0.0
Overseas services (2)	1,772	2,360	33.2	0.7	0.8
MAFF	536	483	-9.9	0.2	0.2
IBAP	898	870	-3.1	0.4	0.3
Forestry	47	37	-22.3	0.0	0.0
Agriculture, fisheries, food and forestry (2)	1,481	1,389	-6.2	0.6	0.5
Employment	2,038	2,710	33.0	0.8	0.9
DTI/ECGD/Energy	1,921	1,300	-32.3	0.8	0.5
Other	5	8	69.9	0.0	0.0
Trade, Industry, energy and employment (2)	3,963	4,018	1.4	1.6	1.4
Roads and Transport	2,973	2,663	-10.4	1.2	0.9
Housing	2,304	1,674	-27.3	1.0	0.6
Other environmental services	2,796	2,702	-3.4	1.2	0.9
Education and Science and Arts and Libraries	11,340	12,334	8.8	4.7	4.3
Law, order and protective services	3,547	4,565	28.7	1.5	1.6
Health	10,042	11,281	12.3	4.2	4.0
Personal social services	1,738	2,075	19.4	0.7	0.7
Finance for PCs	3	8	184.9	0.0	0.0
Health and personal social services (2)	11,783	13,365	13.4	4.9	4.7
Social security	27,573	31,700	15.0	11.4	11.1
Nationalised industries EFLs	1,818	311	-82.9	0.8	0.1
Other dept. programmes (3)	13,286	13,682	3.0	5.5	4.8
Adjustments (4)	-415	-3,009	na	na	na
Total other (2)	12,871	10,673	-17.1	5.3	3.7
Planning total + net debt interest +priv proceeds	104,124	112,471	8.0	43.2	39.4

(1) Excluding Nationalised Industries EFLs.
(2) Sum of previous components.
(3) Includes Wales, Scotland and Northern Ireland.
(4) Privatisation proceeds and general allowance for shortfall.

EC contributions

THE CPRS REVISITED

This note reviews developments since 1982 on the proposals set out in the memorandum by the Central Policy Review Staff (CPRS) entitled "Long Term Options" of September 1982.

2. The CPRS made their report in the context of a note by the then Chancellor of the Exchequer entitled "The Longer Term" (C(82)30) which considered the prospects for public expenditure in the longer term and proposed a new and fundamental look at public spending programmes. The CPRS were asked to examine some of the long term options open to the Government, especially as regards the possibilities for major structural changes affecting the larger expenditure programmes.

3. Essentially, therefore, the CPRS concentrated on Health, Education, Social Security and Defence which together then covered about two-thirds of total public expenditure (it is now about 72 per cent). In a nut shell, the CPRS' view for each of these four programmes was as follows :-

a. **Health**. Health care for the bulk of the population should be shifted from the State to privately owned and run medical facility, but this would have to be buttressed with a scheme for compulsory private insurance. As the first steps towards this there should be increased and extended health charges and encouragement to private health insurance.

b. **Education**. In contrast to health it was not realistic to envisage even as a long term option a wholesale privatisation of provision for education in schools at least primary and secondary schools, but more parents should be encouraged to choose the private sector. Immediate objectives were a substantial reduction in resources going to the public sector, compulsory charges for schooling, or for higher education charging the full cost of tuition.

c. For **Social Security**, discretion should be taken to hold increases in benefits below the rate of inflation but keeping open the possibility of allowing beneficiaries a share in increased prosperity when economic conditions improve by increasing benefits ahead of prices.

d. For **Defence**, the CPRS thought that the NATO commitment was too expensive and reflected some failure in the UK to adjust to poor economic performance and a reduced role in the world a specific proposal was made for this.

The CPRS also looked at a wide variety of other possibilities.

4. Paragraphs 1 to 14 of the note below discusses the specific proposals in the fields of Health, Education, Social Security and Defence, and in paragraphs 15 to 41 look at the other ideas discussed.

5. It is not easy to get a fair feel, seen from now, of the worth or efficacity of the CPRS paper, even leaving aside the political row it caused at the time when it leaked. It is easy enough to see that the general thrust of what they were after has been sustained and carried through, but then this is not overly surprising given the re-election in 1983 and 1987 of the Conservative administration, and the broad continuity of the thrust of their policy. Against that actual delivery of the CPRS' proposals in detail has clearly been pretty patchy, with no moves at all being made in some areas (eg health), moves broadly to the same end but rather in a different manner in other areas (eg education), and many events and shifts that have had happened which was simply not forecast or not forecast as to the scale on which they occurred (eg privatisation). As an instigator and forecaster of change at the retail level, therefore, the CPRS report perhaps ranks low. Against that, however, it would clearly not be fair to suggest that the work done was not useful, or that it did not have some kind of effect on Ministerial thinking.

CONFIDENTIAL

REVIEW OF SPECIFIC PROPOSALS MADE BY CPRS IN 1982

SUMMARY

Proposal	Para below	Position
Health		
More charging	1 and 2	Still on table
Compulsory insurance	3 and 4	-do-
Education		
Cut spending	5 and 6	Not pursued as such
Parents pay more	7 and 8	-do-
Charge degree students	9 and 10	Not pursued
Social Security		
Uprating below prices	11 and 12	Not pursued
Defence		
Cut forecast spending	13 and 14	Achieved anyway
Public Service Manpower		
Cut Civil Service numbers	15 to 18	Broadly achieved
Cut NHS and LA numbers	19 to 21	Some action
Accounting changes		
Reclassify LA spending	22 and 23	Similar changes planned
-do- NIF spending	24 and 25	Not pursued
Other suggestions		
Housing	26 and 27	Reductions anyway
Other LA services	28 and 29	Contracting out pursued
Privatisation	30 and 31	Gone ahead fast
Regions	32 and 33	Changes made anyway
Employment	34 and 35	Not pursued as such
Territories	36 and 37	Some work done
Export Credits	38 and 39	Some changes effected
Payments to EC	40 and 41	-do-

CONFIDENTIAL

REVIEW OF SPECIFIC PROPOSALS MADE BY CPRS IN 1982

I HEALTH

1982 Proposal

1. "The NHS would remain broadly as now but a higher proportion of costs would be met from charges to patients. Existing charges for drugs, dental treatment and spectacles would be raised, and extended to cover everyone (including children and old people), except those close to supplementary benefit level. A modest charge would be introduced for consulting the General Practitioner, and for hospital outpatient visits. Hospital inpatients would also pay a modest charge (say £5 a day). Total savings would depend on the scheme of charges adopted, but would be unlikely to exceed £1 billion a year, even with a drastic reduction in exemptions."

Comment

2. These ideas of reducing exemptions and of charging for consulting General Practitioners and for hospital outpatient visits have not been adopted (apart from the recent decision to extend charging for sight tests and dental examinations), but remain on the table for possible future consideration.

1982 Proposal

3. "The working population would be obliged by law to obtain insurance to cover the costs of health care for themselves and their dependants. Premiums would relate to the family's risks, not their means, and so the poor would need help with meeting the costs. Either initially or later the scheme could be extended to cover the non-working population, who would obviously need much more subsidy."

Comment

4. The idea of compulsory private health insurance, to replace the NHS for the working population, has not been adopted, but remains on the table for possible future consideration.

II EDUCATION

1982 Proposal

5. "Spending on compulsory education for 5-16 year olds would be cut by about £1 billion a year while every effort would be made to maintain essential standards."

Comment

6. This was not pursued. It would have amounted to a reduction of some 13 per cent in schools' expenditure which then ran at about £7½ billion. As the CPRS note made clear, it could only be done with "new powers of central control, with a fall-back power to take over the functions of LEAs." In that sense we can safely say that this proposal is no longer on the table. In the event, LA relevant current expenditure on schools has risen by 13 per cent in real terms between 1982-83 and 1987-88, spending per pupil has risen even further: by 18 per cent in real terms up to 1986-87 (the latest year for which unit cost figures are available). The main reasons have been :

a. the lags and inefficiencies inevitable in managing gradually declining rol~~e~~s with a public duty to provide universal schooling;

b. teachers' pay (also up by 13 per cent real);

c. while teacher numbers have fallen by some 4 per cent, the PTR has also fallen from 18.1 to 17.1.

1982 Proposal

7. "Parents able to afford it would be required to pay the cost of their children's education, whether in the State system (where schools would be required charge fees which covered their costs) or in competing private schools. It would still be compulsory to have children educated, normally at a school which met statutory minimum educational standards. Those with incomes too low to afford to pay would either have fees rebated or (preferably) would be subsidised via some form of income support."

Comment

8. This was not pursued. In the radical consideration of education policy which preceded the development of proposals now in the Education Bill, as well as in the exercise on charging for local government services, it was explicitly assumed that mainstream education would continue to be provided free. In that sense, this proposal was considered and rejected.

1982 Proposal

9. "A significant saving could be achieved by charging degree students at universities etc for their degree courses. The size of this saving would depend on the amount of State assistance it was decided to make available to higher education students; but £1 billion a year could be saved by charging the full cost of degree courses, while still providing assistance in the form of scholarships and/or State-guaranteed loans to, say, 300,000 students (the exact number of students who could be assisted for the same cost would depend on the way this assistance was distributed as between scholarships and loans)."

Comment

10. This was not pursued. The review of student support in 1985 was conducted on "expenditure neutral" assumptions. The current review of student support is based on a "no extra" rule.

III SOCIAL SECURITY

1982 Proposal

11. "The present laws which require most benefits to be increased annually by at least as much as prices would be repealed. New legislation would bring these benefits into line with the present arrangements for child benefit: upratings would become a matter of discretion for the Secretary of State who would attempt to preserve their real purchasing power but only as far as economic circumstances permit. If desired the Government could take the opportunity during the first year of operation of the new legislation to uprate some or all benefits by amounts which would

effect substantial, once-for-all cuts in the real value of benefits. The bolder these initial cuts were the less need there would be in future years to hold down upratings below the level of inflation."

Comment

12. Any political possibility of not fully uprating the pledged benefits seems to have receded since 1982 perhaps due to the widening gap between prices and earnings. Instead, the problem is to resist pressures to uprate by more than prices. There is also pressure to extend the pledge to other benefits. However, the Government has continued occasionally to uprate certain non-pledged benefits by less than inflation or not to uprate at all as eg child benefit this year. Something over half of total benefit expenditure is subject to the pledge.

IV DEFENCE

1982 Proposal

13. "LPTE projections assumed that defence spending would increase in volume terms by 3 per cent a year from 1982-83 until 1988-89, with 1 per cent a year thereafter. The United Kingdom commitment to the 3 per cent growth target currently runs only to 1985-86. The proposal is to maintain the 1985-86 level in real terms, which would save about £1½ billion a year by 1990-91 as against LTPE. Internal forward planning in the Ministry of Defence currently assumes no growth in the defence budget after 1985-86. Hence this option could be achieved either by providing for no additions to spending at present planned, or by reductions to make room for some inescapable additions, eg by cancelling Trident. But the present planning assumption is deliberately cautious, to allow for some flexibility, so it does not follow that the option could be achieved without affecting military capabilities."

Comment

14. The CPRS proposal was for an increase in volume terms of 3 per cent a year to 1985-86 and then to maintain the 1985-86 level in real terms. This would have produced the following run (using actual 1985-86 spend as the base and using Autumn Statement deflators):

	1985-86	1986-87	1987-88	1988-89	1989-90	1990-91
						£m cash
	17,954	18,500	19,286	20,154	20,860	21,485
The run in the forthcoming PEWP is :						
	17,954	18,149	18,850	19,208	19,950	20,560
difference	-	(351)	(436)	(946)	(910)	(925)

This means that while the CPRS proposal was not carried through, something significantly more radical was achieved. The CPRS proposals have effectively been dismissed although something of the sort still lingers in the hearts of many in MOD. (It should be noted that the LTPE exercise assumed the 3 per cent continuing beyond 1985-86, thus gives figures even bigger than CPRS figures.)

V PUBLIC SERVICE MANPOWER ETC

Proposal

15. "Ministers would decide on a target for further reduction of Civil Service manpower, by say 10 per cent during the next Parliament. This would entail giving a high priority to -

- reducing functions, contracting out etc;
- simplifying policies and procedures (tax, social security etc);
- legislation where necessary to achieve these changes;
- expenditure on information technology.

The overall reduction would be allocated among departments and services according to the scope for such changes."

Comment

16. By 1983 the Government had accepted it would be unrealistic to expect further manpower reductions to continue at the previous rate. Nevertheless the net reduction between 1 April 1983 and 1 October 1987 was nearly 64,000 or 9.8 per cent. (The overall manpower targets for

1 April 1984-1987 were all met.) The reduction in manpower due to contracting out, hiving off and privatisation is estimated to have been around 68,000. The main emphasis in the control and planning of departments' use of resources on their cash provision for running costs although a close interest is retained in the trend of Civil Service numbers. Departments are now to build on the financial management improvements progressively introduced in recent years by reflecting in their forward planning of running costs a commitment to progressive annual efficiency gains equal to at least 1½ per cent. Pay has been ratchetted down against earnings elsewhere and the pay system made more flexible.

17. Since 1982 a number of measures to simplify policies and procedures have allowed significant staff savings about 5,000 in the Inland Revenue. These have included the introduction of mortgage interest relief at source (MIRAS), the introduction of a composite rate of tax on bank deposits and changes in departments' procedures on PAYE work. Similarly the 1985 Review of Social Security led to changes which will in due course give substantial staff savings.

18. Central Government expenditure on information technology rose by 15-20 per cent per annum in the early 1980s, 10-15 per cent in recent years and is expected to rise at about 10 per cent per annum over the next 3 years. The central Government spend on IT in 1986-87 was some £1.6 billion and is expected to total around £1.8 billion in 1987-88. This offers benefits in a variety of ways, increasingly in effectiveness and efficiency terms and also contributes to manpower reductions.

1982 Proposal

19. "Similar targets [to those for Civil Service manpower] would also be set for reduction in NHS and local authority manpower. These could be linked with increasing contracting out and privatisation of services."

Comment

20. In the NHS, the total number employed has fallen since 1982, owing to a sharp fall in ancillary staff: "front line" staff (nurses, doctors

etc) have continued to rise. There are no longer centrally imposed targets for reductions in management costs as a proportion of NHS resources, but the Regional Health Authorities set their own targets (subject to scrutiny by DHSS and monitored through the Ministerial Accountability and Review process); and there are continuing targets for efficiency savings of a more general sort in the hospitals service.

21. Ministers did not introduce targets for reductions in local authority manpower, although new arrangements to monitor manpower were set up. Local authority manpower was broadly stable after 1982, but since 1986 has been increasing by about 1 per cent a year. The Government has powers at present to control directly only uniformed police establishments and the manpower of joint boards and other authorities set up after the abolition of the GLC and metropolitan counties. Only the police powers are used (to implement agreed increases). Manpower targets for individual local authorities could be a useful weapon to control LA current spending (the bulk of which is pay), although greater control over pay rates would be at least equally valuable. As a direct means of influencing expenditure, the Community Charge system after 1990 will re-empasise a spending norm for individual authorities, with all spending in excess of the authority's assessed need (GRE) falling solely on local charge payers.

VI ACCOUNTING CHANGES

1982 Proposal

22. "Local Authority Expenditure. Local authorities at present have a large degree of automomy, including the right to spend more than the Government's current spending target if they raise the money locally (by rates) to pay for it. Ministers have been considering this in MISC 79. If they decide not to impose direct central control over current spending, there is a case for counting as "public expenditure" only that part of local authorities' spending which is not financed from local revenues - as for nationalised industries and water authorities now, and local authorities in many other countries. This would be easier

to justify if there were a limit on Exchequer grant, and non-domestic rates, so that expenditure beyond those limits was entirely a "charge" on local ratepayers/electors for extra services provided; both these changes are under consideration in MISC 79."

Comment

23. Ministers decided initially to pursue rate-capping, but subsequently, it was decided to introduce the community charge and the national non-domestic rate. There is agreement in principle between Treasury, DOE and the Prime Minister that a new planning total (comprising CG spending, CG grants to LAs, plus LA borrowing) should be introduced within a framework in which medium-term objectives are set for general Government expenditure, and taxation and borrowing at a national level. This is not the same as the CPRS proposal as that involved treating locally financed expenditure as outside the Government's public spending framework. The current proposal still implies central Government concern about the level of local government spending and taxes (charge capping will supersede rate-capping) but it changes the way the plans to deliver the broad objectives are framed.

1982 Proposal

24. "More than half of social security payments are met from contributions to the National Insurance Fund. This will increase with the new State pension scheme, where public expenditure will vary according to the number "contracted out". In other countries contributory benefits are often treated "off-budget" rather than as part of public expenditure. The case for such a change would be stronger to the extent that contributions are regarded as different from, ordinary direct taxation, and as buying an "entitlement" to benefits."

Comments

25. The proportion of social security payments met from National Insurance Contributions has actually fallen slightly since 1982, owing to the growth in certain non-contributory benefits (supplementary benefit, housing

benefit and disability benefits). The idea of reclassifying National Insurance Fund expenditure, so that it does not count as public expenditure, has not been pursued since 1982. There are strong reasons against it: for example, it would be purely an accounting change and be seen as such; and one of the main reasons for trying to contain public expenditure is in order to be able to cut direct taxes and thus increase incentives and freedom of choice, but National Insurance Contributions have the same adverse effect on incentives and freedom of choice as income tax, so should not be excluded from the picture.

VII OTHER SUGGESTIONS

1982 Proposal

26. "Housing - £2.9 billion - has been falling, but the future trend depends mainly on the real level of rents (as well as rate of sales, new building and improvements); a review of rent policy, and of relating subsidy to current rather than historic values, might be worthwhile (though most of the savings would not count as public expenditure)."

Comment

27. There has been a substantial real terms reduction in net public expenditure on housing since 1981-82, mainly as a result of buoyant receipts from the Right to Buy. The CPRS report was therefore right to highlight the importance of the rate of sales; but further increases in receipts now largely depend on movements in house prices rather than Government initiatives. Local authority rent levels have remained low and largely static in real terms since 1981-82. Subsidy relates to the cost of housing after rent income is taken into account and rents have not been required to meet the current cost of housing provision. A review of housing policy last year concluded that local authorities should be forced to move to current cost rents by progressive withdrawal of subsidy. But housing benefit costs would have been high (some 60 per cent of rents are met by benefit) and, while they accepted in principle the case for economic rents, Ministers decided collectively to leave pressure for rent increases for decision in successive Surveys. A 5

per cent real terms rent increase has been built into subsidy assumptions for 1988-89 but no decisions have been taken beyond that.

1982 Proposal

28. "Other local authority services - £10 billion - there may be more scope for increased contracting out and for charging, analogous to charging for education."

Comment

29. Small extensions have been made to the coverage of the 1980 legislation on Direct Labour Organisations, requiring local authorities to put more construction and maintenance work out to tender. The Local Government (Competition) Bill now before Parliament will require local authorities to contract out services, if it is economic to do so. The primary legislation covers six services (£2.5 billion) and can be extended to cover other services by secondary legislation. Ministers have also decided to allow local authorities to charge for more services and the necessary primary legislation is being prepared.

1982 Proposal

30. "Nationalised industries - £2.3 billion: - privatisation will generate once-for-all gains, but where industries sold are self-financing will have a nil or negative effect on total EFLs thereafter; - continuing deficits might be removed or reduced in the longer-term, but this is bound to be a difficult and piecemeal process."

Comment

31. The privatisation programme has gone full steam ahead since then removing several self-financing industries, including some with negative EFLs. This will continue with increasing effect - Steel, Water and, in particular, Electricity - and the loss of these negative EFLs will put up the total for the remaining nationalised industries. Since 1982 deficits have been eliminated in many industries through higher prices, productivity gains and rationalisation. But Coal and Rail together continue to absorb significant grant (cash figures of £1.7 billion estimated in 1987-88, as in 1982-83, despite Rail's successful efforts at reduction).

1982 Proposal

32. "Regional - counting together expenditure by the Departments of Industry and Environment, this is of the order of £1 billion a year, and is already being reviewed."

Comment

33. The CPRS paper valued the regional programmes of the Department of Industry plus expenditure by the Department of the Environment on urban development at around £1 billion a year. Regional industrial incentives were substantially altered in November 1984, with increased emphasis on selective grants and links with job creation. Further changes to regional policy including the abolition of automatic regional development grants were announced on 12 January 1988 as part of a package giving greater financial control. Regional spending is now under £500 million per annum. Regional spending is now under £500 million per annum. On the other hand expenditure by the Department of the Environment on urban development has grown substantially since 1982 (largely as a result of the expansion of Urban Development Corporations).

1982 Proposal

34. "Employment - £2.2 billion - much of this reflects policy reactions to the state of the labour market and will continue to do so; but there might be some scope for review;

- the Youth Training Scheme might take the place of the last year of compulsory schooling, instead of following it;

- on the training side, a remissible training tax on employers would reduce public expenditure;

- on employment services, privatisation of job centres might be examined."

35. DE Group expenditure was £2.4 billion (on today's definition) in 1982-83, and is planned to be £4.2 billion in 1988-89. As predicted, the increases reflected policy reactions to the state of the labour market.

With falling unemployment, the tide may have turned; savings were made in PES 1987. The measures proposed by the CPRS were not adopted. YTS has been expanded, but instead of a one year scheme substituting for the last year at school, there is now a 2-year scheme with guaranteed places for all unemployed school leavers. In addition, MISC is spending almost £100 million a year to take vocational education into the schools. It would be difficult to reconcile an overall reduction in initial vocational education and training with Government policy (but savings are looked for on YTS for other reasons). A remissible training tax has not been explicitly rejected by Ministers collectively - certainly not since 1985, but it is not a serious runner. There are other obstacles to public expenditure savings on adult training, which are being overcome as far as possible. Wholesale privatisation of Jobcentres might run counter to EC obligations and would be inconsistent with the recent action to amalgamate them with unemployment benefit offices; but smaller privatisation and charging measures in the area of job matching are now under consideration.

1982 Proposal

36. "The territories - Extra spending in Scotland in relation to needs has been investigated in the past, and is probably not worth a further full scale review."

Comment

37. Further work on extra spending in the territories in relation to needs has been done since 1982, and has begun to affect perceptions (within the Government and outside) of the level of Scottish provision. Treasury Ministers have recently decided to set aside for the time being the possibility of a further full scale needs study.

1982 Proposal

38. "Export Credits - the LTPE figure of £0.3 billion does not reflect the full extent of commitments and there may be scope for review."

Comment

39. The CPRS were not specific about the scope for review. Work since 1982 has resulted in some reduction in cost on a multilateral basis, but a decision not to proceed unilaterally. Changes in sources and costs of finance and possible moves to greater selectivity remain on the table.

1982 Proposal

40. "Payments to European Communities - £1.8 billion - depend on future negotiations (in which it may be necessary to bring in the desirability of alternative defence savings eg in BAOR."

Comment

41. The negotiations foreseen in 1982 resulted in the Fontainebleau Agreement of 1984, under which the Community's VAT ceiling was raised from 1 per cent to 1.4 per cent but the UK secured a continuing abatement of its net contribution. The Agreement has substantially reduced our budgetary burden compared with what it would otherwise have been; but the net contribution has continued to grow nevertheless and is now running at around £1¼ billion a year, taking one year with another.

110/4 SN 3783/33

CONFIDENTIAL AND PERSONAL

Mowl 5130
to call back

FROM: MRS P TODD
DATE: 2 February 1988

Sorry. Accident!

1. MR MOWL

The main news is that corporation tax was not as buoyant as expected (although it's still well up on the FSBR). Despite this the surplus was bigger than forecast, partly because of another shortfall on expenditure. The increasing expenditure shortfall may herald another downward revision to the estimate of the 1987-88 planning total. [illegible]

cc
Sir P Middleton
Sir T Burns
Mr Anson
Mr Scholar
Mr Sedgwick
Mr Peretz
Mr Watts
Mr Ritchie

Thanks. What happened last year [illegible] spending [illegible] outturn in 1988-89?

2. CHANCELLOR OF THE EXCHEQUER

CGBR(O) AND CGBR IN JANUARY

The provisional outturn for the CGBR(O) in January is a surplus of £6.0 billion, a £0.3 billion higher surplus than was allowed for in the Treasury's Winter Economic Forecast. The estimate of the CGBR(O) outturn is subject to revision before publication on Tuesday 16 February.

2. The provisional outturn for the CGBR(O) assumes a reduction of £300 million on unallocated receipts contained within "other" receipts. This unwinds the large increase in December and reflects the clearance of taxes now incorporated within Inland Revenue receipts for January. Accurate information on this will be available from the Bank of England later in the month and consequential revisions to the CGBR(O) will be notified to you on 9 February when Mr Mowl reports the provisional PSBR for January.

3. The main differences from forecast reducing the CGBR are lower expenditure (by £0.5 billion), and higher national insurance contributions (by £0.3 billion). In addition Custom and Excise receipts, interest and dividend receipts and other receipts were together £0.2 billion higher than forecast. These differences were partly offset by lower Inland Revenue receipts (by £0.7 billion). Preliminary analysis suggests that the shortfall in Inland Revenue receipts is mainly due to lower receipts of Corporation Tax including Advanced Corporation Tax. Corporation Tax receipts in January appear to have been around £6.2 billion.

4. The CGBR(O) in January also reflects the final repurchases of BP shares at a cost in January of £15 million. This cost has been netted off the January figure for privatisation proceeds.

5. In the first 10 months of 1987-88 the CGBR(O) was a surplus of £6.0 billion. The Budget profile was for borrowing of £0.2 billion. The main factors underlying the shortfall were:

(a) higher Inland Revenue receipts (by £2.6 billion) mainly Corporation Tax (up by nearly £1 billion, including Advanced Corporation Tax), Income Tax (up by nearly £1 billion, mainly on PAYE) petroleum revenue tax and stamp duties (both up by £0.3 billion);

(b) higher Customs and Excise receipts (by £0.8 billion), mainly VAT;

(c) higher national insurance contribution (by £0.4 billion);

(d) higher other receipts (by £0.3 billion), half of which is due to an increase on the balance held on behalf of the European Communities.

(e) a shortfall on departmental expenditure of £1.8 billion. This is measured on a cash basis and reflects a lower view of expenditure than that of departments in their APEX returns.

6. On-lending to local authorities and public corporations in January totalled £0.1 billion. The provisional CGBR in January was therefore a surplus of £5.8 billion. The CGBR since 1 April is a surplus of £3.0 billion.

7. Further analyses of the outturn in January will be given in the next Ministerial note on the PSBR in two weeks' time.

Phillippa Todd

MRS P TODD

110/4 sn 3783/32

CONFIDENTIAL AND PERSONAL

CENTRAL GOVERNMENT TRANSACTIONS

£ billion

	January 1988			April-January 1988			April-January 1987
	Provisional outturn	**Last month's forecast**	**Difference**	**Provisional outturn**	**Budget profile**	**Difference**	**Outturn**
Receipts							
Inland Revenue	12.0	12.8	- 0.7	54.7	52.2	2.6	48.7
Customs and Excise	3.9	3.8	0.1	37.0	36.2	0.8	34.0
National Insurance Contributions	2.8	2.5	0.3	22.7	22.3	0.4	21.1
Privatisation proceeds	- 0.1	- 0.1	-	5.0	5.0	-	3.3
Interest and Dividends	0.5	0.4	0.1	6.9	6.9	-	6.8
Other receipts	- 0.2	- 0.4	0.1	3.1	2.8	0.3	2.4
Total receipts	18.9	19.1	- 0.2	129.4	125.3	4.1	116.3
Expenditure							
Debt interest payments	2.0	2.1	- 0.1	13.6	13.8	- 0.2	13.5
Departmental expenditure (a)	10.9	11.3	- 0.4	109.8	111.6	- 1.8	105.0
Total expenditure	12.9	13.4	- 0.5	123.4	125.4	- 2.0	118.5
CGBR(O)	**- 6.0**	**- 5.7**	**- 0.3**	**- 6.0**	**0.2**	**- 6.1**	**2.2**
CGBR(O) excluding privatisation proceeds	**- 6.0**	**- 5.8**	**- 0.3**	**- 0.9**	**5.1**	**- 6.1**	**5.5**
On-lending to LAs	-	0.1	- 0.1	3.3	1.7	1.7	3.8
On-lending to PCs	0.1	0.1	-	- 0.4	- 0.1	- 0.2	- 0.1
CGBR	- 5.8	- 5.5	- 0.3	- 3.0	1.7	- 4.7	6.0

(a) on a cash basis, net of certain receipts

+ = higher receipts, and higher borrowing, higher expenditure
- = lower receipts, and lower borrowing, lower expenditure

110/4 sn 3785/33

Ch/ I am sorry this CONFIDENTIAL took so long to appear. When I chased Mr Mowl for an answer we discovered - with horror - that he had already replied and the minute had got mislaid in the works of our office. Mustn't happen again. Doubly sorry because this is really just a provisional response and looks pretty inadequate now. More to come on the 18th - PSBR etc.

FROM: COLIN MOWL
DATE: 4 February 1988

CHANCELLOR

cc Sir P Middleton
Sir T Burns
Mr Anson
Mr Scholar
Mr Turnbull
Mr Sedgwick
Mr Ritchie
Mrs P Todd

Thanks. I will take the 18/2 submission ASAP.

CGBR(O) AND CGBR IN JANUARY MPW 12/2

Miss Wallace's minute of 3 February asked what implications another downward revision of our estimate of the 1987-88 planning total outturn would have for expected spending outturn in 1988-89.

2. The Winter Economic Forecast included an overspend on the PEWP planning total for 1988-89 of about £1 billion. As Mr Anson mentioned at your meeting on the forecast on Monday this is broadly consistent with GEP's view of total claims on the Reserve based on a trawl of expenditure divisions' views. We shall be reviewing the forecast, in consultation with GEP, over the next week or two and reporting a revised view to you on 18 February in a submission on the prospects for the PSBR in 1987-88 and 1988-89. This submission will also seek provisional decisions on what PSBR figures should be published in the FSBR.

3. The implications of a larger underspend this year for next year will depend on where the underspend has occurred. At present we have only a very limited breakdown of expenditure in January, although we do know that £0.1 billion of the £0.4 billion underforecast of departmental spending was on national insurance benefits. An underspend on demand-led expenditure such as social security would probably mean that spending would be lower next year too. If the larger underspend were on cash limited spending however it might, in general, have less implications for next year, with the possible exception of an underspend on defence. If, under the end-year flexibility arrangements, MOD carried more spending forward into next year than currently assumed (and did not carry on equivalent extra amount into 1989-90), a larger underspend this year could mean a higher level of expenditure next year.

4. Mr Sedgwick, Mr Turnbull and others will be looking carefully at these issues before reporting a revised view of both this year and next year.

Colin Mowl

COLIN MOWL

CONFIDENTIAL

FROM: A J C EDWARDS
DATE: 4 February 1988

CHANCELLOR

cc: Paymaster General
Sir P Middleton
Sir G Littler
Mr Anson
Mr Lankester
Mr Bonney
Mr Mercer
Mr Mortimer
Mr Evans
Mr Kaufmann
Mr Tyrie

Ch/
Content for the enclosed note to go forward to Mr Lavelle, for circulation to Ministers concerned? *
JF 5/2
yes

STRUCTURAL FUNDS AND BUDGET DISCIPLINE ON NON-COMPULSORY EXPENDITURE (NCE)

Mr Taylor's minute earlier today reports Sir Geoffrey Howe's view that it will not be possible in the final rounds of the future financing negotiation to contain the increase in the structural funds within 1½ times the maximum rate for non-compulsory expenditure (NCE). Sir Geoffrey had already raised with me in Brussels the question which you too have now asked: in such a scenario, how could we best retain some element of effective control and budget discipline?

2. The first point to be made, I think, is that the battle to limit the increase in NCE to 1½ times the maximum rate is not yet lost. We are doing our utmost to stiffen the French and Germans.

3. That said it is all too probable, as Sir Geoffrey Howe says (and as also noted in my minute of yesterday), that the French and Germans will make further concessions on the structural funds, thus making it difficult for the Prime Minister to hold out in isolation.

* Mr Edwards would like to add a further para. to the note, which would point out that we do need a discipline of this sort in addition to the own resources ceiling. JF 5/2
OK

4. If this does happen and the European Council does in effect go beyond 1½ times the maximum rate, the best way ahead would, I think, be:

(i) to seek agreement with the European Parliament to specified limits on the increases in the structural funds and the rest of NCE over the period to 1992; and

(ii) on the assumption that no such agreement is forthcoming, to insist that the Council must agree now not to exceed specified totals for the increase in NCE in the annual co-decision negotiations with the European Parliament.

5. The attached note offers a more detailed assessment. Unless you see objection, we would propose to offer it to Mr Lavelle for circulation to the Ministers concerned along with a note from DTI discussing the implications for the UK of various hypotheses as to the total increase in the structural funds and the degree of concentration on the least prosperous member states or regions.

6. On a minor point, may I apologise for using the term "non-compulsory" rather than "non-obligatory", which I know you prefer. The problem is that "non-compulsory" is now the standard term in all Community texts, and we risk confusing the Prime Minister and others if we use two different terms to describe the same thing.

NCE may be correct in English. But the fact is that everybody uses the French term, DMO.

25/2

AJCE

A J C EDWARDS

CONFIDENTIAL

BUDGET DISCIPLINE FOR NON-COMPULSORY EXPENDITURE (NCE)

Note by the Treasury

Ministers have asked us to consider how the growth of non-compulsory expenditure could best be contained, and an element of budget discipline preserved, if the European Council should decide to concede a much larger increase in the structural funds than the UK would wish.

1.5 times maximum rate case

2. If the agreed real increase in the structural funds over the period to 1992 were around 50 per cent or less, the best way to preserve an element of budget discipline would be for the Council to commit itself to limiting the increase in NCE to 1½ times the "maximum rate" of increase in NCE laid down in the Treaty. This limitation would probably be compatible with growth of about 50 per cent in real terms in the structural funds and growth of other NCE in line with the calculated "maximum rate".

3. Within this broad approach, the best solution would be for the Council to agree that in no circumstances would the increase in NCE exceed 1½ times the maximum rate. The southern member states and Ireland would however undoubtedly reject this on the grounds that they would have no assurance that the actual increase in expenditure on the structural funds would be as great as the Council intended.

4. The second best solution would be to provide that the growth of NCE would be contained within 1½ times the maximum rate of increase unless a higher rate of increase was needed to finance the total sum obtained by adding the agreed increase in the structural funds to a "maximum rate" increase in other NCE. This solution would best be encapsulated in a text along the lines of the attached Annex, with paragraph 15(c) included.

Beyond 1.5 times maximum rate case

5. If the agreed real increase in the structural funds is significantly over 50 per cent, it would no longer be convincing to pretend that the total increase in NCE could be kept within 1½ times the calculated maximum rate. The Council would have to accept that, in accordance with Article 203 of the Treaty, the overall rate of increase in NCE would fall to be determined by agreement between the Council and the European Parliament. In this "co-decision" scenario, there would no longer be any rate of increase in NCE on which the Council could formally insist on the basis of Article 203 of the Treaty.

6. In these circumstances, the best way which we have been able to identify for preserving an element of budget discipline would be for the Council to decide that:

(i) for its part, it intended the structural funds to grow by n per cent or by specified annual amounts (eg 60 per cent or 1 becu a year) between 1989 and 1992 and the rest of NCE by a rate equal to the calculated maximum rate as laid down in the Treaty;

(ii) the Council would seek a binding agreement with the Parliament not to exceed these increases in the two broad components of NCE;

(iii) failing such agreement with the Parliament (and failure would be virtually a forgone conclusion), the Council would commit itself to limiting the amount of the total increase in NCE throughout the co-decision negotiations with the Parliament each year to the sum of the agreed structural funds increase and the maximum rate of increase for the rest of NCE, without any commitment as to the structural funds and "other NCE" components individually.

This approach is reflected in the draft Council conclusions at the Annex, though with paragraph 15(c) omitted.

7. The thinking which underlines (b) and (c) above is that, if there should be a binding agreement with the European Parliament on maximum levels of expenditure for the structural funds and the rest of NCE, then the Council could reasonably commit itself to specific amounts of growth for these two components separately (see paragraph 16 of the draft conclusions).

8. If on the other hand there were no such agreement with the Parliament, but the Council had committed itself to a stated increase in the structural funds, the Parliament would have power under the Treaty to allocate massive sums to NCE other than the structural funds, and the Council would then have to raise its total allocation for NCE so as to fulfil its obligations on the structural funds. That is why in the "no agreement" scenario it would be important for the Council to avoid any absolute commitment to specific increases for the structural funds on their own.

9. In practice, the Parliament would doubtless hold out in the budget procedure each year for a larger increase in NCE than the Council's self-imposed limitation implied. The Council would however have committed itself to this limitation. ~~That~~ The Council's nerve might sometimes crack before the Parliament's; but there is no way in which we can guarantee to prevent this happening in advance.

A "lawnmower" provision

10. Another potential hazard is that the Council, which now has a southern as well as a northern blocking minority, might find itself unable to reach agreements on individual budget lines which were compatible with the agreed limits on the total growth of the structural funds and other NCE. In that event there would be some danger that the other northern member states in the Council would crack sooner than the southern member states. The "lawnmower" provision in paragraph 18, based on a Council conclusion of 1979, would deal with this problem. The UK's advocacy of such a provision has not so far, however, met with much success.

4 February 1988

COUNCIL CONCLUSIONS ON BUDGET DISCIPLINE FOR NCE

15. The Council for its part intends to apply the provisions of Article 203 so as to respect the following principles:

(a) progression of commitment appropriations for the structural funds in accordance with [Chapter II, paragraph 8] of these conclusions [ie increases of M becu in 1988 and N becu in each of the following years up to 1992];

(b) progression of commitment appropriations for NCE other than that referred to in (a) above not to exceed the maximum rate of increase communicated by the Commission;

*[(c) the total increase in NCE to be contained each year throughout the budget procedure within 1½ times the maximum rate of increase communicated by the Commission. The Council will propose an increase in this rate only if this is needed to cover the sum of the amounts implied by (a) and (b) above.]

16. In accordance with the June European Council agreement that the Fontainebleau budget discipline arrangements must be strengthened, and with the European Parliament's wish for a binding accord on budget discipline between the twin arms of the budgetary authority, the Council will aim to reach a firm agreement with the European Parliament on the implementation of these expenditures as set out above over the whole period up to 1992.

17. If no such agreement is possible, the Council within the framework of Article 203(9) of the Treaty will consider the sum of the amounts at (a) and (b) above as a maximum during all the budget procedure.

*[18. If, in the course of the budget procedure, the Council is unable to agree on amounts of non-compulsory appropriations on individual lines which would enable the total amounts at (a) and (b) above to be respected, the Commission's proposals (at first reading) or the Parliament's amendments (at second and subsequent readings) will be adjusted by common percentages so as to make the provisions on individual lines consistent with these total amounts.]

19. The Council will adopt decisions accordingly at the same time as the own resources decision.

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* Highly desirable provisions which may in practice be non-negotiable.

RM2.76

CONFIDENTIAL

pmp

PSF 21/3

PSF 20/4

22/4

FROM: MOIRA WALLACE

DATE: 8 February 1988

MR ANSON

cc Chief Secretary
Sir P Middleton
Sir T Burns
Mr Kemp
Mr Odling-Smee
Mr Spackman
Mr Turnbull
Mr Call

Ch/ shall we fix a meeting to discuss X? MPW 22/4

PS8 fix an early mtg with Mr Scholar. M

LONGER-TERM PUBLIC EXPENDITURE

The Chancellor was most grateful for your note of 2 February, covering papers by Messrs Spackman, Turnbull, and Kemp. He has commented that these are a most interesting half-term report. Apart from the overriding need to concentrate now on health, as Mr Anson points out, the Chancellor wonders if anything can be done to curb the number of teachers. X The Chancellor is also attracted by the possibility of an up-dated version of the 1984 Green Paper: this would be worth discussing after the Budget.

MPW.

MOIRA WALLACE

3785/3

CONFIDENTIAL AND PERSONAL

FROM: COLIN MOWL
DATE: 9 February 1988

Mrs 9/2

1. MR SCHOLAR

2. CHANCELLOR OF THE EXCHEQUER

cc Sir P Middleton
Sir T Burns
Mr Peretz
Mr Sedgwick
Mr Ritchie
Mrs Todd
Miss H Chapman

Thanks. I shd be grateful if PEM and Sedgwick the v. different math of the publication of this figure. NL

PS. When will answer to my questions of 3/2? NL

PSBR IN JANUARY

The first provisional outturn for the PSBR in January is a surplus of £6.3 billion, a £0.2 billion higher surplus than was allowed for in the Winter Economic Forecast. The average of City forecasts currently available is a surplus of £4½ billion, with a range of £4 billion to £5¼ billion. The estimated outturn is subject to revision before publication at 11.30 a.m. on Tuesday 16 February. The January figure is the last one to be published before the Budget. The February figure will be published on March 16.

2. There have been some revisions to the earlier months of the year. Compared with last month's press notice the cumulative PSBR to December is £0.2 billion lower than previously estimated. Within this total the LABR is £0.3 billion lower and the PCBR £0.1 billion higher.

3. The provisional outturn for the CGBR(O) in January is a surplus of £5.9 billion, a £0.1 billion lower surplus than the first estimate given in Mrs Todd's minute of 2 February. Mrs Todd's minute (copy attached) also provided an explanation for the difference between the January outturn and forecast and for the cumulative difference from the Budget profile.

4. The LABR in January was a surplus of £0.1 billion. This is a somewhat lower LABR than seen in January for each of the two previous years (possibly representing a partial unwinding of the unusually high LABR in December) but is similar to the average in the 3-4 years prior to that. The PCBR in January is provisionally a surplus of £0.4 billion, broadly in line with last year's figure but lower than the years before that.

5. The PSBR in the first 10 months of 1987-88, a surplus of about £7 billion, is £6¾ billion below the Budget profile (£6 billion is lower than expected CG own account borrowing)

and £7½ billion below the level of the PSBR in the same period of 1986-87. Excluding privatisation proceeds, the PSBR in the first 10 months of 1987-88 was £6¾ billion below profile and £5¾ billion below the same period last year.

6. The monthly note, providing a fuller explanation, will be circulated next Monday, 15 February. As with last month's note it will not contain forecasts of the remaining months of the year. Instead these will be included in Mr Sedgwick's submission on the 1987-88 and 1988-89 PSBRs on 18 February.

Colin Mowl

COLIN MOWL

3785/3

CONFIDENTIAL AND PERSONAL

	January 1988			April 1987-January 1988			April 1986-January 1987
	Provisional outturn	Last month's forecast	Difference	Provisional outturn	Budget forecast	Difference	Outturn
CGBR(O)	- 6.0	- 5.7	- 0.2	- 5.9	0.2	- 6.1	2.2
LABR	- 0.1	- 0.3	0.2	0.1	0.1	-	- 0.6
PCBR	- 0.4	- 0.1	- 0.2	- 1.1	- 0.4	- 0.7	- 1.1
PSBR	- 6.3	- 6.2	- 0.2	- 6.9	- 0.2	- 6.7	0.5
PSBR excluding privatisation proceeds	- 6.3	- 6.2	- 0.1	- 1.9	4.8	- 6.6	3.8

5-50

CONFIDENTIAL AND PERSONAL

FROM: COLIN MOWL
DATE: 12 FEBRUARY 1988

I agree

1. SIR PETER MIDDLETON

2. CHANCELLOR OF THE EXCHEQUER

I agree that 6 (ii) is the only viable presentation.

cc Economic Secretary
Sir Terence Burns
Mr Scholar
Mr Sedgwick
Mr R I G Allen
Mr Bush
Mr Ritchie
Ms Chapman

DRAFT PRESS BRIEFING ON PSBR IN JANUARY

... I attach the draft press briefing on the PSBR in January.

2. The estimate of <u>the PSBR in January</u> to be published Tuesday is a surplus of £6.3 billion, the same figure as the first estimate I reported on 9 February.

3. Available <u>City forecasts</u> are for a surplus in a range £4 billion to £5¼ billion, with an average of £4½ billion. The outturn is therefore a higher surplus than expected in the City. After last month's figures the reported City view was that a surplus of £1-2 billion for 1987-88 as a whole was likely. With a cumulative surplus to January of £6.9 billion, analysts are now likely to conclude that the 1987-88 surplus will be at least £3 billion.

4. We have considered carefully with Mr Scholar and IDT how we should react when asked to comment on this likely City view. We have combed through the figures, looking for special factors to which we could plausibly point in attempting to damp down comment. There are two possibilities:

(i) The size of the end-year surge is a major uncertainty. We can make something of this. But the largest recorded deficit for February and March together was £3.8 billion in 1982-83, equivalent to £4.8 billion at today's prices. Even if this record level of borrowing were repeated, and there are no special factors to which we can point to suggest that this will happen, the surplus for the year would be £2 billion.

(ii) The LABR is, as always, subject to great uncertainty (and is running this year so far at £¾ billion above its 1986-87 level). But there is no evidence we can point to in order to suggest that the LABR end-year surge is likely to be larger than usual, and the 1986-87 comparison could easily backfire on us.

5. Against this background we have concluded that it is not possible to sustain last month's line that it is too early to say whether the PSBR will turn out lower - or higher - than the Autumn Statement forecast. IDT advise that to try and argue that the Autumn Statement forecast might not be undershot would make the Treasury look silly and could give rise to press stories to that effect.

6. In these circumstances we have identified two possible options:

(i) no comment apart from "new forecast in the Budget" (justified by the Budget being only a matter of weeks away);

(ii) Autumn Statement forecast now looking likely to be undershot. But still major uncertainties about the eventual outcome. Main uncertainties are size of end year surge in central government expenditure and local authority borrowing. New forecast in Budget.

7. There is a third, radical, option: given that everyone will now be expecting a surplus, that we should make a virtue of this expectation, saying - taking our cue, perhaps, from Prime Minister's question time, where we may expect this to come up in a Health Service context - that the Government's prudent stewardship has brought about the situation in which the National Debt seems likely to be smaller at the end of the year than at the beginning. The advantage of this is that it might lead people to revise downwards their guesses of tax reductions next year (prudence, clearly, being the order of the day). The disadvantage is that it might give rise to a new spate of overheating stories, with "Now Treasury forecasts surplus" headlines.

This is Michael Scholar's idea (which he himself thinks is not on)

8. All in all this seems too risky an option - and one which might, anyway, achieve the wrong result. Between options (i) and (ii) in paragraph 6 we prefer the latter, as looking less defensive, and allowing us to make one or two points - on the surge and the local authorities uncertainties - which may have some minimal impact.

9. We would not offer this option as our initial comment, but would use it as a response to the inevitable follow-up question about the prospects for the year as a whole. Our initial comment, volunteered to Reuters, would be the usual recital of the latest monthly figure and the cumulative comparison with last year, as follows:

> "PSBR in January provisionally a surplus of £6.3 billion. Excluding privatisation proceeds, PSBR for first 10 months of 1987-88 was a surplus of £1.8 billion, as compared with borrowing of £0.8 billion in same period of 1986-87."

Conclusion

10. We should be grateful, during the course of Monday morning, for guidance as to which of the options in paragraph 6 you wish us to adopt and for any other comments on the draft briefing.

Colin Mowl

COLIN MOWL

From: ALLEN RITCHIE
16 February 1988

MR R.I.G. ALLEN - IDT

MR LANG - CSO Press Office

cc List A

Chancellor
Chief Secretary
Financial Secretary
Paymaster General
Economic Secretary
Sir P Middleton
Sir T Burns
Mr Anson
Mr Monck
Mr Scholar
Mr Peretz
Mr Sedgwick
Mrs Butler
Mr Grice
Mr Mowl
Miss O'Mara
Mr Pickford
Mr Bush
Mr Franklin
Mrs Todd
Mr R Evans
Miss Chapman
Mr Mansell - CSO
Mr Richardson - CSO
Mr Wright B/E
Mr Gray - No 10

List B
(distributed at 11.30am, 16 February)

Mr C.M. Kelly
Mr Cropper
Mr Tyrie
Mr Call
Mr Ko - IR
Mr Balley - C and E

BRIEFING FOR 16 FEBRUARY PSBR PRESS NOTICE

The PSBR figures for January will be published at 11.30am on 16 February. The provisional outturns, together with figures for the first ten months of 1986-87 and 1987-88, are shown in Table 1. Cumulative figures for the PSBR and its components for 1985-86 and 1986-87 are shown in Table 2 overleaf. Table 3 shows outturns excluding privatisation proceeds.

Table 1: Borrowing requirement outturns

£ billion

	Apr 1986 -Jan 1987	Apr 1987 -Jan 1988	Jan 1988
Central government on own account	2.2	-6.0	**-6.0**
Local authorities	-0.6	0.1	**-0.1**
Public corporations	-1.1	-0.9	**-0.2**
PSBR	0.5	-6.9	**-6.3**
Memo: PSBR (excluding privatisation proceeds)	3.8	-1.8	-6.3

Note: Figures may not sum precisely because of rounding.

Table 2: PUBLIC SECTOR BORROWING REQUIREMENT – Comparison with the last two years

Cumulative £ billion

	Central government on own account			Local authorities borrowing requirement			Public corporations borrowing requirement			Public sector borrowing requirement		
	1985-86	1986-87	1987-88	1985-86	1986-87	1987-88	1985-86	1986-87	1987-88	1985-86	1986-87	1987-88
Apr	1.1	0.2	**1.9**	0.8	0.7	**0.5**	-0.2	-0.1	**-0.4**	1.8	0.8	**2.0**
May	2.3	1.9	**2.2**	0.8	0.4	**0.1**	-0.4	-0.5	**-0.4**	2.7	1.8	**1.9**
Jun	2.7	3.1	**1.7**	0.5	-0.1	**0.2**	-0.5	-0.7	**-0.5**	2.6	2.3	**1.4**
Jul	3.6	3.1	**1.4**	0.8	-0.1	**0.4**	-1.2	-1.0	**-0.8**	3.1	1.9	**0.9**
Aug	4.6	4.2	**2.3**	0.9	0.2	**0.2**	-1.2	-0.8	**-0.9**	4.3	3.6	**1.6**
Sep	5.1	6.7	**2.0**	1.1	0.0	**0.5**	-0.7	-0.9	**-0.7**	5.6	5.8	**1.8**
Oct	5.0	6.5	**1.5**	0.7	-0.3	**0.1**	-0.5	-0.5	**-0.8**	5.3	5.7	**0.8**
Nov	6.2	7.3	**0.5**	0.1	-0.7	**-0.5**	-0.3	-0.9	**-0.8**	6.0	5.7	**-0.8**
Dec	7.4	5.7	**-0.0**	0.4	-0.6	**0.1**	-0.2	-0.9	**-0.7**	7.6	4.2	**-0.6**
Jan	2.9	2.2	**-6.0**	0.5	-0.6	**0.1**	-0.2	-1.1	**-0.9**	3.2	0.5	**-6.9**
Feb	2.9	2.3		0.4	-0.7		-0.6	-1.5		2.8	0.1	
Mar	4.3	4.5		1.7	0.2		-0.2	-1.4		5.8	3.4	

Note: Figures may not sum precisely because of rounding.

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(DRAFT)

Table 3: PUBLIC SECTOR BORROWING REQUIREMENT EXCLUDING PRIVATISATION PROCEEDS

Cumulative £ billion

	Central government on own account			Local authorities borrowing requirement			Public corporations borrowing requirement			Public sector borrowing requirement		
	1985-86	1986-87	1987-88	1985-86	1986-87	1987-88	1985-86	1986-87	1987-88	1985-86	1986-87	1987-88
Apr	1.1	1.3	**2.1**	0.8	0.7	**0.5**	-0.2	-0.1	**-0.4**	1.8	1.9	**2.2**
May	2.5	3.0	**2.9**	0.8	0.4	**0.1**	-0.4	-0.5	**-0.4**	2.9	2.9	**2.6**
Jun	4.0	4.2	**4.1**	0.5	-0.1	**0.2**	-0.5	-0.7	**-0.5**	3.9	3.4	**3.8**
Jul	5.0	4.2	**4.3**	0.8	-0.1	**0.4**	-1.2	-1.0	**-0.8**	4.5	3.0	**3.9**
Aug	6.2	5.3	**5.7**	0.9	0.2	**0.2**	-1.2	-0.8	**-0.9**	5.9	4.7	**5.0**
Sep	6.8	7.8	**6.0**	1.1	0.0	**0.5**	-0.7	-0.9	**-0.7**	7.3	6.9	**5.8**
Oct	6.7	7.5	**4.8**	0.7	-0.3	**0.1**	-0.5	-0.5	**-0.8**	7.0	6.8	**4.1**
Nov	8.2	8.6	**5.4**	0.1	-0.7	**-0.5**	-0.3	-0.9	**-0.8**	7.9	7.0	**4.1**
Dec	9.7	8.9	**5.1**	0.4	-0.6	**0.1**	-0.2	-0.9	**-0.7**	9.9	7.5	**4.5**
Jan	5.1	5.5	**-1.0**	0.5	-0.6	**0.1**	-0.2	-1.1	**-0.9**	5.4	3.8	**-1.8**
Feb	5.2	6.0		0.4	-0.7		-0.6	-1.5		5.1	3.8	
Mar	7.0	9.0		1.7	0.2		-0.2	-1.4		8.5	7.8	

Note: Figures may not sum precisely because of rounding.

CONFIDENTIAL AND PERSONAL
(DRAFT)

CONFIDENTIAL AND PERSONAL
(Until 11.30am 16 February 1988)

SUMMARY OF LINE TO TAKE

PSBR in January provisionally a surplus of £6.3 billion. Excluding privatisation proceeds, PSBR for first 10 months of 1987-88 was a surplus of £1.8 billion, as compared with borrowing of £3.8 billion in same period of 1986-87.

1. January PSBR

Background
City forecasts of January are for a surplus in a range from £4 billion to £5¼ billion. Average is a surplus of £4.4 billion.

Line to take
January PSBR always a surplus - main month for mainstream corporation tax. CT receipts for January provisionally totalled around £6 billion (1986-87 - just under £5 billion).

2. PSBR, April-January

Line to take
Excluding privatisation proceeds, PSBR in first 10 months of 1987-88 was a surplus of £1.8 billion, as compared with borrowing of £3.8 billion in 1986-87. Local authorities borrowing, however, running at level higher than last year (see Q.11).

3. PSBR undershoot on Autumn Statement forecast for 1987-88?

Background
Forecast for 1987-88 revised in Autumn Statement to £1 billion, (£3 billion lower than forecast at Budget time). City commentators have said that this is still an over forecast and that PSBR likely to be in surplus for 1987-88.

Line to take
Autumn Statement forecast now looking likely to be undershot. But still major uncertainties about the eventual outcome. Main uncertainties are size of end year surge in central government expenditure and local authorities' borrowing. New forecast in Budget.

4. Privatisation proceeds in 1987-88

Background

Privatisation proceeds so far this year £5.1 billion, compared with £3.3 billion in same period last year. Autumn Statement figure for 1987-88 as a whole £5 billion, unchanged from FSBR forecast. Costs of privatisations offset the gross privatisation proceeds, so quite feasible that total for year as whole could be slightly lower than cumulative total to end-January. No further instalments from earlier privatisations scheduled for the remainder of 1987-88.

Line to take

Net privatisation proceeds in January were close to zero.

5. Effect on PSBR of BP share support scheme

Background

BP share support scheme closed on 6 January. Treasury press notice on 7 January said that cost of Issue Department purchases of BP shares was around £27 million (around 39 million shares at 70p each). Purchases in January - counted in January PSBR - around £15 million.

Line to take

Negligible effect on PSBR.

6. Consolidated Fund Revenues

Background

Press notice shows that Consolidated Fund (CF) revenues in first ten months of 1987-88 were 11½ per cent higher than in the same period last year, comprising 12½ per cent increase in Inland Revenue receipts, 8½ per cent increase in Customs and Excise receipts, and 19 per cent in "other revenues". "Other revenues" include privatisation proceeds when they are transferred into Consolidated Fund - these amounts may differ from total privatisation proceeds given in table 5 of press notice. Proceeds received by HMG are usually transferred to Consolidated Fund with a lag.

No forecast of Consolidated Fund revenue given in Autumn Statement, but total taxes on income, expenditure and capital in 1987-88 forecast to be £2.3 billion higher than in FSBR. These were forecast in the Autumn Statement to increase by 8¾ per cent compared with 7 per cent in the FSBR. See Autumn Statement para 1.57 for composition of additional receipts.

Line to take

Consolidated Fund revenues in April to January £103.5 billion, 11½ per cent up on same period last year. Includes some privatisation proceeds. Excluding privatisation proceeds revenues up by 10 per cent.

7. Inland Revenue Receipts

Background

Inland Revenue receipts in January £12.0 billion. Total for April-January £54.7 billion, (12½ per cent up on same period last year). FSBR forecast for year as whole was a rise of 7½ per cent on 1986-87. More detailed monthly figures will be published later in Financial Statistics, Table 3.13. No forecast of total Inland Revenue receipts given in Autumn Statement, but stated that North Sea revenues £0.6 billion higher, income tax about £½ billion higher and Corporation tax about £¾ billion higher than in FSBR.

Line to take

Receipts in April-January £54.7 billion, 12½ per cent up on same period last year. January receipts include around £6 billion corporation tax (provisional estimate) (1986-87 - just under £5 billion).

8. Customs and Excise Receipts

Background

Customs and Excise receipts in January £3.9 billion. Total for April-January £37.0 billion (8½ per cent up on same period last year). FSBR forecast for year as whole was a rise of 6½ per cent on 1986-87. More detailed monthly figures will be published later in Financial Statistics, Table 3.14. No forecast for Customs and Excise receipts given in Autumn Statement, but stated that VAT about £½ billion higher than in Budget forecast.

Line to take

Receipts in April-January £37.0 billion, 8½ per cent up on same period last year.

9. Supply Expenditure

Background

FSBR gave a figure for provision for supply in 1987-88 but not a forecast of outturn because public expenditure Reserve was not allocated to individual components of expenditure, (but public expenditure total used in PSBR forecast assumed that the Reserve was fully spent).

Line to take

Provisional outturn for supply expenditure in January £8.8 billion. Total April-January 1987-88 (provisional £85.8 billion) up 3½ per cent on same period last year. Excluding advance contributions to EC Budget paid from supply in 1986-87, increase is 4½ per cent.

10. Central Government Borrowing

Background

CG own account borrowing in January, surplus of £6.0 billion. Total for April-January, a surplus of £6.0 billion (1986-87, borrowing of £2.2 billion). Privatisation proceeds, April-January, £5.1 billion (1986-87, £3.3 billion).

Line to take

Excluding privatisation proceeds, CG own account borrowing over April to January lower by £6¼ billion than same period last year.

11. Local Authorities

Background

LABR (provisionally) a surplus of £0.1 billion in January (zero borrowing in January 1987). Local authorities recorded borrowing of £0.1 billion during first ten months of 1987-88. (Surplus of £0.6 billion for same period in 1986-87). Some revisions to earlier months - see Q.13.

Line to take

LABR for first 10 months of 1987-88 around £¾ billion higher than for same period in previous year.

12. Public Corporations

Background

PCBR (provisionally) a surplus of £0.2 billion in January. Surplus of £0.9 billion over April to January. (Surplus of £1.1 billion, April-January, 1986-87, but aggregate then included BGC, for most of year, and BA).

Line to take

PCBR so far in 1987-88 little different from last year.

13. Revisions to last month's estimates

Background

PSBR for April-November revised upwards last month by £0.4 billion. Main factor - upward revision of £0.5 billion to LABR, reflecting revisions to data on LA short-term financial assets. Further revisions this month on same account, plus usual three-monthly revisions on receipt of full quarterly information. This month's revisions partly reverse last month's.

Line to take

PSBR for April to December revised downwards by £0.2 billion since last month. LABR revised down by £0.3 billion and PCBR revised up by £0.1 billion. Revisions reflect incorporation of full quarterly information for Q4 on LA and PC borrowing, and changes to data on LA short-term financial assets.

Allen Ritchie (270-5029)
PSF Division, HM Treasury

Reference……………………………………………

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V helpful on the presentational issue. X opens the way to 'at the same time' publications, wh. wd make the much easier for the publication of Y (the residual) in the form of Written Answer (or a series of written answers), thus avoiding a separate publications. And Z makes the clear that the replacement for the PEWP debate wd be debates on Dept'l reports & estimates wh wd be taken by Dept'l (& not Tsy) MMs!

2. On other pts: the Chancellor's complaint was about the Revenue determines expenditure doctrine, Rawlinson, wh argues that it does not mean that Revenue constrains expenditure; it is the expenditure that determines the Revenue total. It constrains not a rate of Revenue wh. allows for the fiscal [illegible] (Quite a good report.)

3. The RPIS proposals must be totally rejected. A thoroughly retrograde [illegible] [illegible].

N.

FROM: MISS C EVANS

DATE: 15 February

MR TURNBULL

cc Chancellor
Chief Secretary
Paymaster General
Sir Peter Middleton
Mr Anson
Mr Kemp
Miss Pearson
Mr Odling Smee
Mr Hawtin
Mr Brigner
Mr Gilmore
Mr Grieve
Mr Saunders
Mr R I G Allen

Ch/

(1) Quite helpful on AS/PEWP etc (but X on p6 will not please Mr T).

(2) Makes much too much of "revenue determines expenditure". When did Gov't last use phrase?

(3) V long & boring

AA

TCSC DRAFT REPORT ON THE PEWP

I attach a copy of the draft report on the PEWP. As usual this has been sent to us on a confidential and informal basis for factual checking. It should not be revealed that we have it. Could I have any comments/corrections to be passed to the Clerk by close tomorrow pl.

C Evans

CODE 18-77

IN CONFIDENCE

TREASURY AND CIVIL SERVICE COMMITTEE

Chairman's draft Report

Contents

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revised draft GC 11/2/88

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The Government's Public Expenditure Plans 1988-89 to 1990-91

Chairman's draft Report

Introduction

1.During our inquiry we heard evidence from the Rt Hon John Major, Chief Secretary to the Treasury, and from Treasury officials. A number of supplementary notes from the Treasury are appended to the evidence, as are papers by our advisers, Professor Andrew Likierman and Mr Terry Ward. We are most grateful both to our witnesses and to our advisers. [Papers from the British Aggregate Construction Materials Industries and the British Road Federation are also appended.]

2.In recent years the Committee has used its inquiries on the Autumn Statement and the Budget to consider macro-economic policy. We intend to continue that practice and accordingly this Report concentrates more narrowly on a number of specific issues raised by this year's Public

Expenditure White Paper. We recognise, however, that the foundations upon which the Government's spending plans are based - particularly as they relate to future years - will be affected by the Government's ability to maintain stable economic conditions. These are issues we expect to deal with in our Report on the forthcoming Budget. In the meantime, in this Report we deal in particular with the content and format of the White Paper and its relationship with the other financial documents which are put before the House; with the process whereby the planning total and figures for departmental spending are arrived at and may subsequently be modified; with arrangements for allocations from the Reserve; with the relevance to decision-making of information about indices of inflation linked specifically to the spending of individual departments; with the assessment of performance and "outputs" (ie what the taxpayer is buying with given amounts of public money). We also deal with running costs and with capital expenditure.

PART 1

FORM AND CONTENT

3.The 1988 Public Expenditure White Paper continues the practice established over the years of providing more and better information about public expenditure. This year Volume 1 has been considerably expanded. In addition to the customary Summary chapter on the Government's expenditure plans Volume 1 now contains three chapters which were previously contained in Volume II, the chapters on "Additional Analyses", "Local Authority Public Expenditure in Great Britain", and "Public Corporations" together with a new chapter on "Historical Trends". A sixth chapter contains information on presentational differences between this year's White Paper and its immediate predecessor. Volume II is concerned exclusively with Departmental spending plans which now receive greater coverage than in previous years. It also contains an index for both volumes.

4. Despite the improvements in presentation contained within the White Paper, many of which have occurred as a result of recommendations made by our predecessor Committee, there is still considerable scope for improvement. A number of problems remain and some of these are discussed in later sections of this report, for example, in relation to measures of departmental performance. We recognise that the more information that is provided the more questions may arise. An example of this is the new Table 6.1 at page 106 of Volume I which summarises differences from last year's White Paper by department. That Table reveals sizeable changes in outturn figures for both 1986-87 and 1987-88 as compared with last year's forecasts, but it does not explain, as we believe it should the principal reasons for these changes.

5. In the last Parliament the Committee recommended a number of possible changes in the way in which the House deals with the major financial documents presented by Government. The Committee proposed, for instance, that it would be better if select committees could comment on the material at present in the departmental chapters of the White Paper in time for a debate in the early summer rather than in late February.[1] The Committee also proposed that Volume II of the White Paper be split up into a number of departmental reports.[2] In this report we draw attention to the overlap between the Autumn Statement and much of the material which this year appeared in Chapter I of Volume I of the White Paper. We share the Chief Secretary's view that since the Autumn Statement has taken over the role of presenting public expenditure aspects of macro-policy it had clearly downgraded the importance of the Public Expenditure White Paper as published at present.[3] We were pleased to note that he was "very happy to look sympathetically" at translating elements of Chapter 1 of the White Paper into the Autumn Statement.[4] While he was evidently less sympathetic to the proposal to split Volume II of the White Paper into separate departmental reports his mind was clearly not closed to that proposition. We welcome his readiness to consider changes, because despite the many improvements in presentation of information (which the Committee's previous reports have acknowledged) we believe the time is now ripe to propose to the House and

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1. 3rd Report, 1985-86, HC 192 para 2
2. 2nd Report, 1984-85, HC110, paras 12, ?74-75. See also 7th Report, 1984-85, HC323 and 3rd Report, 1986-87, HC153 para 24
3. Q96
4. ibid

Government a new scheme for dealing with the Government's annual expenditure plans.[5]

6. Our starting point is that the House as a whole and its select committees wish to have the earliest and fullest information on the Government's plans in order to have an opportunity to influence succeeding public expenditure rounds. Since the Autumn Statement now contains so much information about departmental spending plans for future years we think it should come to be seen as the key public spending document. It is after all published shortly after the completion of the main public spending round and it announces the main figures for departmental spending[6] which are usually little modified in the period before the PEWP is published only two months or so later.

7. After reviewing the existing position we recommend that in future an expanded Autumn Statement should include the material now in Chapter 1 of Volume I of the White Paper. We recommend also that instead individual Departments should publish their own forward-looking annual reports including the kind of financial information at present included in the departmental chapters of Volume II of PEWP but considerably expanded, to take account however of the other points mentioned in this report. The White Paper in its present form would then be dropped as a separate exercise. Since we are asking that more complete information than that which now appears in the departmental

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5. Particularly since the Government is committed to providing a further response to the Eighth Report of Session 1986-87 from the Committee of Public Accounts on "Financial Reporting to Parliament", Q7. The Treasury Minute in reply to that Report was published in July 1987 as Cm 177
6. together with many departmental press notices

chapters of Volume II of the PEWP should be included in these annual reports we would expect them to be published rather later than January as PEWP now is. They should nevertheless be published no later than the end of the Easter recess[7] to allow time for study of them by the House and its committees. The basic financial information in these annual reports would follow a standard pattern agreed with the Treasury, and all departments should give the fullest possible information on objectives, targets and performance indicators and on their success in meeting these. Otherwise there should be no central editorial control of other material in them. These reports ought thus to include figures of outturn for the financial year just ending, could take account of any adjustments at the time of the budget and could give a full account of any reasons why performance had either failed to reach, or had exceeded, previously set objectives and targets, as well as setting explicit targets for future years.

8.The development of such annual departmental reports would have important advantages for Parliamentary accountability. It will also have important practical advantages as compared with the information now included in Volume II of PEWP. The sheer size of the present publication has been given as a reason for not putting more material into what is already an unwieldy document.[8] Much additional information is regularly made public by departments either in the form of regular memoranda to select committees (such

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7. Here our emphasis is different from that of the PAC which suggested publication of departmental reports in the Autumn alongside the Appropriation Accounts for the previous year (PAC 8th Report, 1986-87, HC 98, para 30)
8. Q60, and see PAC 8th Report 1986-87, HC98 Q384

as those provided by DHSS) or in the form of annual reports on specific parts of their activities.[9] A considerable part of this kind of material could be included in new departmental reports, thus making them comprehensive in their coverage.

9. At the same time as these detailed departmental plans are published or preferably earlier, the Treasury should in our view publish a document which would be the rump of Volume I of the present PEWP and would include the analysis of public spending by spending authority, by function and by economic category and information about running costs, privatisation, science and technology etc. which this year comes after Chapter 1 of that volume.

10. We believe that these proposals would provide important advantages for the House and its select committees. To summarise:

a. The main public spending information would be available at the end of the PES round in the autumn.

b. The House and this Committee could consider not only the macro-economic context, which has been a feature of our recent reports on the Autumn Statement, but could reflect on the balance between departmental programmes.

c. Select Committees generally would be able to consider

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9. See the list of almost 200 regular publications on the plans and performance of departments and some of the main non-departmental public bodies showin in Annex B to the Treasury Minute in reply to the report by the Committee of Public Accounts on "Financial Reproting to Parliament" (Cm177)

annual reports which would be more "user-friendly" and more informative than the departmental chapters of the PEWP and would represent a significant improvement in parliamentary accountability.

d. The detailed study by select committees of these annual reports of departments setting out both past achievements and detailed future plans would provide an excellent parliamentary viewpoint for the next PES round. The future policy and future spending plans and commitments of departments are one of the main interests of departmental select committees, as they seek to establish the Government's provisional plans for the future <u>before</u> final commitments are made.

11.A number of problems would need to be resolved. We were told, for instance, that while "all the big numbers" can be announced easily in the autumn, a number of programmes were at that stage settled only at "a fairly aggregate level and there are still details in sub-programmes to be settled".[10] There were further difficulties about "the territories whose programmes are settled by reference to what happens in England"[11]. These problems could we suggest be solved by separate publication, as early as possible, and certainly no later than at present, of any figures missing from the new Autumn Statement.

<u>Examination of financial documents</u>

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10. Q2
11. ibid

12.Alongside our recommendatons about the publication of financial information, we wish to set out our thinking on how the House might, in this new situation, debate the Government's spending plans. Clearly these suggestions affect many interests in the House and what follows should be seen only as a suggested scheme to form the basis for further discussion.

13.At present there is a full day's debate first on the Autumn Statement and then on the Public Expenditure White Paper. Both of these debates follow, usually within only a few days, reports by this Committee. Under our proposals we would obviously expect an early debate on the new fuller Autumn Statement. Select Committees generally would be able to begin to attempt to influence the new PES round. Here we note that the first stage in the re-assessment of priorities in the new Survey is carried out by Ministers and officials <u>within</u> departments (usually in March and April) before any proposals are put forward for collective consideration.[12] With more accessible material to hand with which to scrutinise the work of departments, select committees may be in a better position to make bids for Estimates day debates.

14.Our proposals may thus lead to an increased demand for Estimates days of which there are of course only three as compared with the eight proposed by the Select Committee on Procedure (Supply) in 1981.[13]. We believe that there may

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12. See Government reply to the Committee's Report on the 1987 White Paper, First Special Report, 1986-87, HC335, apge iii
13. HC(1980-81)118

also be a case for additional time to be made available to debate motions proposed by select committees arising out of their scrutiny of the new annual departmental reports. Such debates would be more sharply focussed than those on the usual motion to "take note" of a Committee's Report, but would also be able to range more widely than debates on a particular Vote in the Estimates. Motions expressing an opinion on the Government's future spending would not be restricted by the rule that limits amendments on Estimates to motions to reduce spending. Such debates would also perhaps be a valuable alternative to the present, frequently unsatisfactory debate on the PEWP, which if the logic of our earlier recommendations were carried through would disappear. The White Paper debate has never been one of the most popular debates in the House, to a considerable extent it is sandwiched between the debate on the Autumn Statement and the impending Budget which greatly inhibits what Treasury Ministers will say. Clearly these are matters which have important implications for other interests in the House including other departmental select committees, the Liaison Committee, and the usual channels. They will no doubt wish to consider our proposals before final decisions are reached.

15. For convenience we now set out in tabular form what we see as a possible revised timetable for the financial year.

October/November: Expanded Autumn Statement presented

November onwards:	Hearings by Treasury and Civil Service Committee on the inter-departmental priorities revealed in the Autumn Statement and on the macro-economic context. Other Committees may wish to take note of the overall figures relating to the departments which they monitor.
January/February:	publication of detailed Treasury analysis of spending figures, viz Chapters 2 to end of this year's Volume I; and of detailed spending figures not available at the time of the Autumn Statement.
March/April:	Budget; publication of MTFS; publication of annual departmental reports including detailed financial information on outturn for previous year and detailed plans for future years and summary of departmental Estimates.
April/May/June:	Consideration by departmentally related select committees of these annual reports and Main Estimates.
May/June:	Possible new debates arising from select committee scrutiny of annual reports.

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June/July: Debates on main Estimates.

16. Finally we continue to hope that, whatever changes may be made in the financial documents presented to Parliament, the Government will recognise the importance of relating
5 its three year forward plans and objectives to the annual Estimates through which the House is able to exercise detailed control of Government spending.[14]

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14. See, eg, 3rd Report, 1986-87, HC153, para 7

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In confidence

TREASURY AND CIVIL SERVICE COMMITTEE

Chairman's draft report on PEWP

PART II

THE ESTIMATED OUTTURN 1987-88 AND PLANS FOR 1988-89

17. The monitoring of the extent to which spending plans are fulfilled forms an important part of any expenditure planning process. Table 6.1 of the White Paper gives information about the extent to which the plans in the 1987 White Paper are likely to be realised. According to the latest Treasury estimates government spending is likely to fall short of the planning total set in the 1987 White Paper by approximately £1.3 6 million. Indeed without an "adjustment" of £600 millions, (the difference between the sum of the individual departmental outturns and what the Treasury expects the overall outturn to be)[15], the estimated underspend would have approached £2 billion.

18. A large part of the underspending however is attributable to much higher than expected sales of public sector land and buildings which, despite our continued observations to the practice, Treasury accounting conventions count as negative expenditure rather than as a

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15. Q92

financing item. If the planning total is measured before these are deducted, then the present estimate of shortfall is reduced to only just over £500 million. After allowance for net debt interest payments, which are not included in the planning total, there is hardly any underspending at all.

? (implies higher debt interest payments)

19.However, while the overall outturn differs little from the planning total Table 6.1 also indicates that some individual departments are estimated to have increased spending significantly since the publication of the 1987 White Paper. The programmes for European Communities, Energy, Education and Science, DHSS-Health and personal social services, and DHSS-Social Security all record appreciable increases. No explanation is given for these increases or for the marked reductions in the figures for Agriculture, DOE-Housing, Trade and Industry and Transport. Future White Papers should, we believe, clearly indicate the reasons for major changes such as those shown in Table 6.1. We so recommend.

20.The spending plans contained in this year's White Paper elaborate the summary figures presented in the Autumn Statement. Cash plans for the 1988-89 are £2.6 billion higher than those contained in the 1987 White Paper, or almost £3 billion higher if the total is measured before deducting asset sales. Including the forecast increase of net debt interest, total cash spending is now projected to be £4 billion higher for 1988-89 than the figure in the 1987 White Paper.

THE PLANNING PROCESS

21.This year the Public Expenditure White Paper was published at a time of considerable public debate about public spending in general and spending on the NHS in particular. We have identified three particular areas of concern about the way in which the public expenditure total is determined and distributed between spending departments. These are

(i) the manner in which the overall figure for public spending is determined;

(ii) the way in which spending priorities are determined; and

(iii) the way in which the Reserve is used during the course of the year to fund additional departmental spending.

(i) <u>Determination of the Planning Total</u>

22.The Government claims that there are two criteria governing the overall level of public expenditure. Firstly government spending should fall as a proportion of GDP.

Secondly the overall level of spending should be determined by what the country can afford. Or as the Government has expressed it "Revenue determines expenditure and not the other way round." — give source?

23. While an expenditure target expressed in terms of GDP may be a perfectly reasonable medium term policy aim we consider that in the short term the criterion is so vague as to be almost useless in determining expenditure in any one year. It seems clear for example that for 1988-89 the planning total could have been increased by a further £1 or £2 billion without undermining the criterion. If economic growth turned out to be faster than forecast the scope for additional spending might have been even greater.

24. In practice it seems that the contention that spending should represent a diminishing proportion of GDP plays hardly any role during the planning process in determining the annual expenditure total. When we asked why the planning total for 1988-89 had been fixed at £156.8 bilion the Chief Secretary told us that the figure represented the outcome of the negotiations between himself and the individual spending departments. He said:

"We seek to keep tight control of public expenditure, but we do not seek to keep it so tight and clear-cut as to aim particularly at one percentage point within £1 billion. The final planning total figure is, of course, the outcome of a whole series of different bilateral, in some cases trilateral, and in a few cases quadrilateral discussions between the Chief Secretary of the day and the individual spending departments, and the reason you get what looks superficially as a rather odd total is the aggregate of those individual decisions. We do not specifically aim at £156.8 billion; that is the aggregate that is built up from the outcome of a whole series of individual decisions."[16]

He went on to add that,

"the principal purpose of the negotiations between the Chief Secretary and the spending departments is to determine what we think is the right level of provision we should make for that particular department in the forthcoming three years, and primarily in the immediately forthcoming year, and it is the outcome of those discussions that determines the precise figure for the planning total rather than the relationship between that outcome and the GDP ratio."[17]

25. We are also sceptical about the extent to which revenue actually does determine expenditure. Treasury officials maintained that the revenue projections published along with the Medium Term Financial Strategy were at the heart of the planning process.

"The one thing one wants to appreciate is where the survey

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16. Q99
17. Q100

fits into the general budgetary process. We prefer to see it as starting with the Budget and the MTFS which reviews the prospects for the economy, the prospects for borrowing and taxation, and that is then published in March. Then a Survey takes place against that background. The Survey takes an extremely long time to work through and the results are published in November."[18]

The revenue envelope within which the Public Expenditure Survey for financial year 1988/89 took place was predicated on a revenue forecast for that year made at the time of the 1987 Budget. Since then, however, owing to faster than forecast economic growth, higher company profits, and higher oil prices, revenues have increased substantially.

26.The Chief Secretary explained that the events of the last twelve months were above trend and should be seen "in a proper perspective."[19] He went on to tell us that it was never the normal practice to revise the revenue estimate during the course of the Public Expenditure Survey and adjust planned expenditure accordingly.

"We would only revise the revenue estimates for the medium term once a year, and that would be done at the time the MTFS was published with the Budget. What we do have though ... are short term forecasts that are revised more often than the Medium Term Financial Strategy."[20]

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18. Q34
19. Q106
20. Q106

Nonetheless despite the availability of these short term forecasts for the current financial year expenditure plans were left unaltered. Instead the Chancellor announced a reduction in the estimated 1987-88 PSBR outturn from £4 billion to £1 billion.

27. The Chief Secretary conceded that if the revenue forecast for the next financial year taken at the time of the Budget was more buoyant than expected or was planned for then it was possible to increase spending.[21] Treasury officials pointed out that revisions had been made at the time of the Budget, although these tended to be rare events.[22] In practice however the Chief Secretary thought that such revisions were not consistent with prudent financial planning.

"I suppose the converse of rushing to spend what seems to be increased revenue would be rushing immediately in-year to make very substantial in-year retrenchments if revenue falls short of your expectations. That has happened in the past, as you will recall, but it is not an attractive way to conduct affairs. It is better to have a smoother flow, and to that extent I accept what I suspect is your underlying concern that expenditure provisions tend to follow as a little behind the revenue projections. I would argue that that is a prudent way to proceed in terms of Public Expenditure if one is interested in ensuring that you have a regular and consistent flow of public

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21. Q107
22. Q39

expenditure rather than a jerky pattern, which does no good either for individuals or for programme expenditure plans." 23A

28. But these sentiments seem to be the obverse of the "revenue determines expenditure" criterion. It seems clear that during the current financial year revenues will be substantially greater than were originally forecast at the time of the 1987 Budget. On the government's criterion expenditure could be increased - either during the current financial year on programmes which might need additional funding, such as the NHS, or during 1988-89. Instead there seems to be a presumption that if revenues turn out to be greater than expenditure then lower taxes or lower government borrowing should balance the equation rather than increased expenditure.

23A Q107

(ii) The determination of priorities

29. The way in which spending priorities are determined during the annual Public Expenditure Survey is something which has concerned both ourselves and our predecessors. In our report on the Autumn Statement we reached the conclusion that the mechanism for determining priorities was not working as well as it should. Accordingly during the course of this inquiry we took further evidence on the subject.

30. Our initial understanding of the way in which spending priorities were determined was that they were essentially an outcome of the "bilaterals" conducted between the Chief Secretary and the spending departments during the public expenditure survey. Where agreement could not be reached the area of dispute would be put before the "Star Chamber" or, in exceptional circumstances before the Cabinet. In any event it was the Cabinet which endorsed the agreements reached between the Chief Secretary and the spending departments or any decisions reached by the "Star Chamber". Both the Chief Secretary and Treasury officials told us that the Cabinet itself played a fuller part than we had previously supposed. According to the Chief Secretary, spending priorities for the forthcoming planning period are discussed by the Cabinet during July but this is not the end of its involvement.

"... insofar as priorities are concerned ... priorities are not only discussed in bilaterals, nor are they only discussed at the July and November Cabinets. Priorities are discussed frequently in Cabinet meetings throughout the year, and perhaps in particular when there are specific policy reviews, a large number of which have been carried out in the last two years or so. It is not the case that when one comes to Cabinet everybody is in the position that they have to discuss from the floor upwards, as it were, a whole and complete set of political priorities. Many of those will have been the subject of discussion over many months in bilaterals and in Cabinet sub-committee meetings, and in Cabinet itself, so many of those priorities will be familiar to all colleagues around the Cabinet table."[23]

(iii) <u>"In-year" changes</u>

31. However when it comes to changes in priorities occurring during the course of the year it seems clear that the present system has a number of shortcomings. If during the course of the year an element of a department's expenditure programme assumes greater importance, it is by no means certain that the department concerned will be allocated the funds necessary to fund the extra "priority" spending from the Reserve. If priorities are re ordered "in year" so that spending on one part of a department's programme is allowed to increase that department may be expected to make compensatory savings elsewhere. One recent instance of

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23. Q113 and see Q41-43. This emphasis on the discussion by Cabinet of spending priorities contrasts with the evidence given to our predecessor Committee by the then Mr Francis Pym who said "As far as I know, no such broad review [of public expenditure priorities] has occurred in the lifetime of this Government" (Minutes of Evidence, 30 June 1986, HC(1985-86)285-iii).

last

this was in relation to the latest nurse's pay increase which was only 90% funded from the Reserve.

32. We asked the Chief Secretary why "in year" changes in priority could not be funded by the Reserve or from savings effected in other departments. He told us that while in the first instance he would expect the recipient department to making savings

"it would not necessarily be the case that if we could not find the off-setting savings we would ... deny the extra resources required from the Reserve."[24]

The Chief Secretary told us that cross departmental savings posed additional problems:

"if we were to seek cross-departmental savings, it would destroy one thing that seems to me generally to be rather important for each individual programme in the Government's budget, and that is the consistency in-year for managers of knowing what resources are available to them so that they are able to plan satisfactorily within those resources. If therefore in-year, because I had to find extra resources for one programme, I were to seek a reduction in a different programme, it might not be a cost effective reduction in terms of the effect that it would have on the performance of that particular programme ..."[25]

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24. Q115
25. Q115

But exactly the same reasoning can be used to refute the contention that savings should be found in the department "favoured" by "in-year" changes of priority. We hope that the Chief Secretary will reconsider the position for the future.

THE RESERVE

33.The funding of unforeseen expenditure or of expenditure which has assumed greater priority "in-year" raises a number of questions about the role of the Reserve in the expenditure planning process, and the criteria determining access to it.

34.Table 1.8 at page 12 of the White Paper shows the planning total by department in cash terms. While most departments show some increase in cash terms, if adjusted by the GDP deflator these increases in many cases become decreases or are seen to be very small.

35.In 1988-89, however, the Reserve is set at £3.5 billion. The Reserve for 1988-89 is thus capable of financing real spending growth of almost 2% greater than shown. Since, of course, it is inconceivable that the Reserve will be allocated between departments on a proportional basis, it is difficult to judge by how much actual departmental expenditure will change during the course of 1988-89. The Chief Secretary himself noted that "there is a mirage"[26] in

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26. Q116

the departmental planning totals because they did not include future drawings from the Reserve. We tried to establish the basis upon which drawings could be made from the Reserve. The Chief Secretary told us that

"the Reserve is there to meet the unavoidable, the unexpected, the unplanned and the unforeseeable."[27] While our predecessors criticised the Government in previous years for making inadequate provision for the Reserve, we do not think the information now provided about the present much larger, more prudent Reserve gives a fair indication of probable departmental spending. We do not think that it is satisfactory that an indication is never given that recourse to the Reserve for certain programmes is highly probable.

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27. Q115

PART III

THE RELATIVE PRICE EFFECT

36. In its report on last year's PEWP, the Committee recommended that more information be published on the Relative Price Effects (RPE) borne by departments. In doing so the Committee stressed that it was "very far from undervaluing the importance of cash limits".[28] In its reply, the Government rejected the Committee's proposal saying that it did not have the information with which to calculate the RPE for each programme and the Planning Total as a whole. The Government also argued that publishing RPE information would not be desirable since it would detract from the deliberate emphasis upon cash planning, with its advantages of encouraging managers to restrict cost increases and to be efficient. The Government pointed out that statistical convention would tend to distort RPEs by failing to allow for increases in productivity and insisted that attention should be focused upon outputs not inputs[29]. This year the Chief Secretary told us that the Government stood by these points and argued that to move to RPE as a basis of planning would be to "institutionalise" general and public sector inflation[30].

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28. 3rd Report (1986-87), HC153, para 13-15
29. HC(1986-87)335, piv
30. Qs140-1

37. We understand that RPE information is at present collected by the MoD, the DHSS, for the road programme by the DTp and, for the water industry, by the DOE[31]. Asked what use the Treasury made of this information, an official replied:

"we do not make a great deal of use of" [it][32]

On the other hand the Chief Secretary said that RPE was information which "departments would take into account when they submit their bids"[33].

38. While we understand why the Treasury do not feel that it is appropriate to use RPE data exuante in planning and controlling resources we are convinced that it is a useful means of examining ex post how differential rates of cost increase have affected the distribution of real resources across the public sector.

39. We take the view that the advantages of the publication and use of RPE outweigh the disadvantages highlighted by the Government. Cash planning is now firmly established and the possession of RPE data would not hinder its effective continuance. We believe that accurate RPE information is important for management, consumers and the public.

40. This is not to ignore the fact that, as the Government

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31. Appendix ...
32. Q48
33. Q140

emphasise, inputs are not a reliable measure of output. Various efficiency improvements may mean that financial inputs, even if they are being undermined by inflation, will still be able to deliver a greater level of output. For example, significant improvements have been achieved in the NHS, so that many more patients are treated per bed, per annum than previously. Nevertheless, the technique of adjusting inputs by inflation remains valid as one measure amongst others by which to judge the likely change in public sector outputs.

41. In many cases there are serious problems in measuring final output. Much public sector output, not traded in any market, is difficult to value except in terms of the cost of input. It may also be difficult to quantify changes in some outputs over time. Departments should certainly seek to develop the best possible indicators of output to enable quantitative assessments to be made, even if these indicators fall short of measuring the output well. But, since there are inherent problems in quantifying public sector output, the use of figures adjusted by the best possible pay and prices information is important.

42. Both the cash terms and "real terms" (adjusted by the GDP deflator) tables in the White Paper may be misleading. Additional tables adjusted for individual changes in departmental pay and prices, even given the methodological problems of producing RPE information would provide a useful check. The Chief Secretary said of RPE indices:

"One of the problems with relative price indices, which by no means has been cracked, is how one actually constructs the relative price indices that are fully satisfactory."[34]

Nevertheless, we believe that RPE information, taken together with other data, should provide a better indicator of changes in allocation of "real" resources than either cash terms or cash terms adjusted by the GDP deflator. The picture of expenditure totals proceeding ever upwards in cash terms may possibly give a misleading impression to the unenlightened.[35] The tables in "real" terms, which ought to solve this problem, may also confuse. What these figures show is the cash allocation deflated by the GDP deflator and not the level of goods and services individual departments will be able to buy.

43. The absence of systematically collected RPE data obstructs rational consideration by government and public alike of the way in which resources have been allocated within the public sector. Government should surely take account of RPEs if it is to compare and control the allocation of real resources against policy. Without information on differential inflation rates, the public lacks the best measure by which to judge statements about the growth in public expenditure and its components and, to enter into debate about its size and distribution.

44. While we are sure that the discipline of coping with

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34. Q144
35. The British Road Federation makes this point in its submission to the Committee with regard to the figures used by the DTp for the growth of expenditure on roads (see Appendix ...

inflation is important for departmental managers it nonetheless seems unreasonable to expect departments continually to absorb their own pay and price movements without there being full knowledge of what has been happening. Such a policy will lead to a situation where relative inflation plays a large and arbitrary part in the allocation of real resources. Some departments may lose, while others may gain. This is not rational.

45. In summary, whilst strongly supporting the need for emphasis on outputs and efficiency in the use of inputs, we recommend the greater use of RPE data in the PEWP. Where necessary, a "significant health warning"[36] may need to be added to ensure awareness of the methodological problems in constructing reliable RPE indices.

46. In a wider context we are increasingly concerned at statements by Ministers and others about increases in "real" resources allocated to particular departments and their activities when the figures are based on cash terms adjusted by the GDP deflator which takes no account of relative price effects. We believe that when RPE figures are available they should be used rather than cash figures adjusted by the GDP deflator and - given the large differences between them which may arise - it should be made clear which basis is being used.

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36. Q144

AIMS AND OBJECTIVES

47. The need for aims, objectives, targets and performance indicators was well summarised in last year's public expenditure debate, by the then Chief Secretary:

"I see three main benefits from better measurement and targeting. By relating outputs to the costs involved, managers can make better choices. By setting out in advance what a programme is expected to achieve, by when and at what cost, subsequent review and evaluation is improved. By telling this House and the outside world what has been achieved and how that relates to previous targets, Departments are made more accountable."[37]

48. In its report on last year's PEWP[38], the Committee said, that whilst there had been some improvement on the previous year:

"Nevertheless, the PEWP is still some way short of providing all the information needed to enable an assessment of departments' efficiency and the attainment of government objectives are frequently expressed in general terms, which makes it difficult to verify ex post whether they have been achieved."[39]

While there has been some further improvement, there remains scope for more.

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37. Hansard, 18 February 1987, Col 931
38. HC(1986-87)153
39. para 17

49. We recognise that in some cases, as we were told by a Treasury official, aims at departmental level are necessarily vague[40]. But some of the departmental aims set out in the White Paper seem to us to be little better than statements of the obvious. We were therefore pleased to be told that the Treasury is endeavouring to encourage more tightly drawn aims and objectives within departments[41].

TARGETS AND PERFORMANCE INDICATORS

50. We were told that there are at present some 1800 performance indicators in the White Paper, but the Treasury recognises that many of these are not true indicators relating inputs to outputs[42]. It is ironic that, when the importance of outputs and efficiency is becoming more widely recognised, in many cases outputs remain largely unmeasured. We recommend that further work should be done on quantifiable indicators which can be used on a consistent basis from year to year, enabling them to be monitored regularly to establish how performance compared with plans. These indicators should be clearly specified and appraised in future annual publications.

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40. Q59
41. Q59
42. Q59

RUNNING COSTS AND MANPOWER

51.The resources used in government administration and the civil service have, since 1986-87, been subject to both a running cost control system and a forward manpower target control system. It is the Treasury's view, that this "belt and braces" approach could be modified. The White Paper recalls that during the debate on last year's White Paper the Government announced that

"the main emphasis in the control and planning of departments' use of resources will from 1988-89 be on their cash provision for running costs; and that overall manpower targets would not be set beyond 1 April 1988 although the Government would retain a close interest in the trend of Civil Service numbers."[43]

We note that the downgrading of manpower targets as a control mechanism, in favour of running cost budgeting, could result in greater consistency and flexibility. Our predecessors commented upon the limited coverage of manpower targets which excluded nationalised industries and local authorities. They pointed out that "only 10 per cent of total public service manpower is covered".[44] The move towards primary reliance on running cost budgeting will place the government administration and civil service within the same control regime as the rest of the public sector.

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43. Cm 288-I page 49, para 40
44. para 29 HC153

52.The Chief Secretary told us that the change was intended to give departments greater flexibility in how they use their running costs in order to get best value from them. Whilst acknowledging that "it may in some cases mean more staff", he foresaw that departmental managers, taking advantage of their delegated financial power, would choose their most economical staffing levels, grade mix and the mix of staffing and non-staffing expenditure.[45]

53.Table 2.13 on departmental running costs should, in the future, allow a clear appraisal to be made of the effectiveness of running cost budgets. It would, however, be useful if, when significant increases in running cost budgets are planned, the departments would, as a matter of standard practice, provide a clear explanation. If running costs rise significantly in the absence of new departmental objectives, it is difficult to resist the conclusion that administrative costs are not totally under control. There can, however, be perfectly valid reasons for increases in running costs. For instance, as the White Paper explains, the 13% increase in the running cost budget for Customs and Excise is largely determined by the higher costs associated with the prevention of drug smuggling. However, the White Paper provides no explanation within the text for the 6.9% increase in Inland Revenue running costs. It was not that there was not a good explanation to hand. When questioned, the Chief Secretary told us that the increase resulted from increased workload which was a

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45. Q160

"direct reflection of the fact that there are more people self-employed, considerably more people starting their own small businesses and, of course, rising economic activity." [46]

Without some explanation for the increases in running costs within the text - particularly if these increases are in excess of the forecast rate of inflation - it is difficult for the reader to relate running cost budgets to departmental outputs and to the overall efficiency of the department.

CAPITAL EXPENDITURE

54.Table 2.10 in Volume I of the White Paper shows that central and local authority capital expenditure in real terms is planned to fall between 1987/88 and 1990/91 by 5 per cent and 14 per cent respectively.

55.We asked why successive expenditure plans persistently showed a decline in planned real capital expenditure and the Chief Secretary told us:

"Whilst the programme sets out the present planned capital expenditure over the three year period, there are additions to capital that may come in here from a variety of sources. One of them is that additions to capital may of course come from the Reserve, although in year that is not common (it

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46. Q161

can happen, but it is not common). Capital expenditure usually has a longer lead time, so it does not come out of the Reserve in year. However, there are also increases in capital expenditre that come about in the nationalised industries, for example, if they generate more internal resources or if greater receipts are generated by local authorities. So when you see the outturn for capital at the end of this year, you are lkely to see a larger figure than actually appears in the plans at the beginning of the year. That has historically been the position and is likely to be so in future".[47]

56. Although it is true that additions have regularly been made to plans during the course of successive years, the fact is that in the period 1978-79 to 1986-87 capital spending in real terms fell by 9%[48].

57. We find it difficult to understand, given the gestation period associated with capital expenditure, why under-forecasting persists. Several explanations are possible, for instance, projects may have been omitted from the previous White Paper because of delays in project approval. Lack of information on local authorities and Nationalised Industries capital spending plans or projects running over-budget could be other explanations for capital spending forecasts proving to be inaccurate. We recommend, however, that in the future reasons for significant changes in figures for capital spending should be clearly stated and

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47. Q164 and see also Q82
48. T42

that the Treasury should take further steps to improve the accuracy of its forecasts of capital spending.

55. We recognise that the setting of capital expenditure targets unrelated to specific projects could lead to a misallocation of resources. Funding, for instance, could be approved for uneconomic projects - if the target is set too high - or economic projects could be rejected, on the other hand, solely on the grounds that the predetermined target for capital spending had been reached. Nevertheless, we feel that there may be grounds for questioning whether the investment appraisal techniques adopted may not be unnecessarily stringent.[49]

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49. see Appendix 5

Tony D please

From: COLIN MOWL
15 February 1988

CHANCELLOR

Copy with PPS letter, attached, for:

Mr Gray - No. 10

cc List A | List B (distributed at 11.30am, 16 February)

List A	List B	
Economic Secretary	Chief Secretary	Mr Grice
Sir P Middleton	Financial Secretary	Miss O'Mara
Sir T Burns	Paymaster General	Mr Richardson
Mr Scholar	Mr J Anson	Mr A Hudson
Mr Sedgwick	Mr Moore	Mr Franklin
Mr Peretz	Mr Culpin	Mrs Ryding
Mr Odling-Smee	Mr Turnbull	Mr Cropper
Mr Watts	Mrs Brown	Mr Tyrie
Mrs Todd	Mr Bottrill	Mr Call
Mr Ritchie	Mrs Butler	Mr Calder - IR
Miss Chapman	Mr R I G Allen	Mr Allen - C and E

MONTHLY NOTE ON THE PSBR

I attach a report on the PSBR outturn for January, and a comparison with the Treasury Winter Economic forecast. The January outturn will be published by press notice at 11.30am on Tuesday 16 February.

The note does not contain the usual forecasts. The forecast for the last two months of the year is in the course of review as part of the Budget preparations.

Colin Mowl

COLIN MOWL

PUBLIC SECTOR BORROWING

Summary

- The PSBR in January is provisionally estimated as a surplus of £6.3 billion, a £0.1 billion higher surplus than allowed for in the Treasury's Winter Economic Forecast.

- The surplus for April to December has been revised from £0.4 billion last month to £0.6 billion this month.

- Borrowing is continuing to run well below the levels expected at the time of the Budget. The PSBR for the first ten months of 1987–88, a surplus of £6.9 billion, is £6.7 billion below the Budget profile, of which about £6 billion is accounted for by lower central government own account borrowing.

- Excluding privatisation proceeds the PSBR for April to January is a surplus of £1.8 billion. This is the first time that the cumulative PSBR excluding privatisation proceeds has been in surplus this year. Excluding privatisation proceeds the April to January outturn is about £5½ billion lower than the corresponding period last year and about £6½ billion below the Budget profile.

- The usual forecasts for the PSBR are not presented in this note. The forecast for the last two months of the year is in the course of review as part of the Budget preparations. It is fairly certain that there will be a PSBR surplus for the year as a whole. The Treasury's Winter Economic Forecast put the surplus at £2¾ billion.

Figures in this report are not seasonally adjusted and also may not sum precisely because of rounding.

Chart 1 : 1987-88: Comparisons with 1987 Budget profiles

£ billion cumulative

——— = Estimated outturn in 1987-88
.... = Budget profile

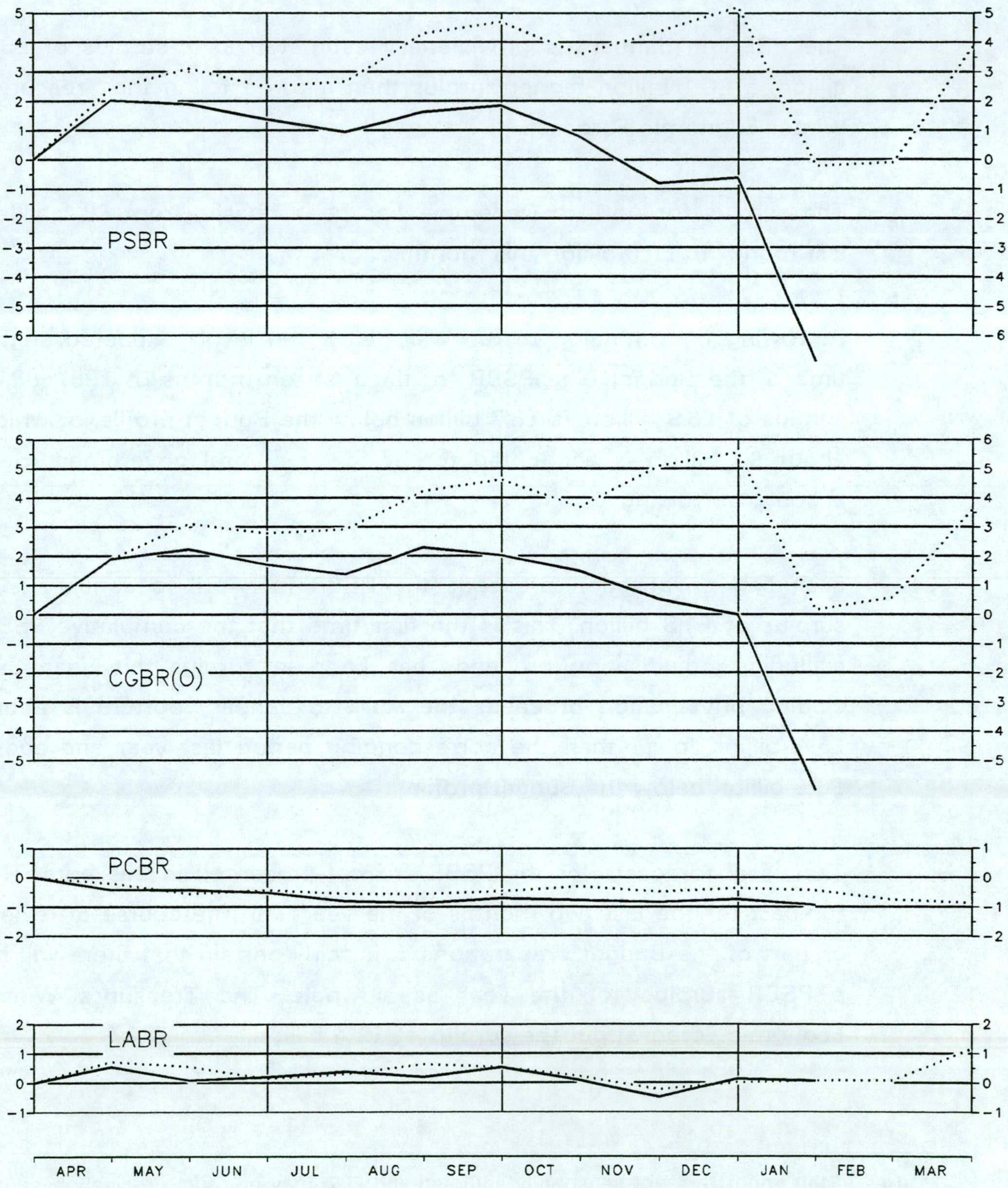


Chart 2: 1987-88: Comparisons with outturns for 1986-87

£ billion cumulative

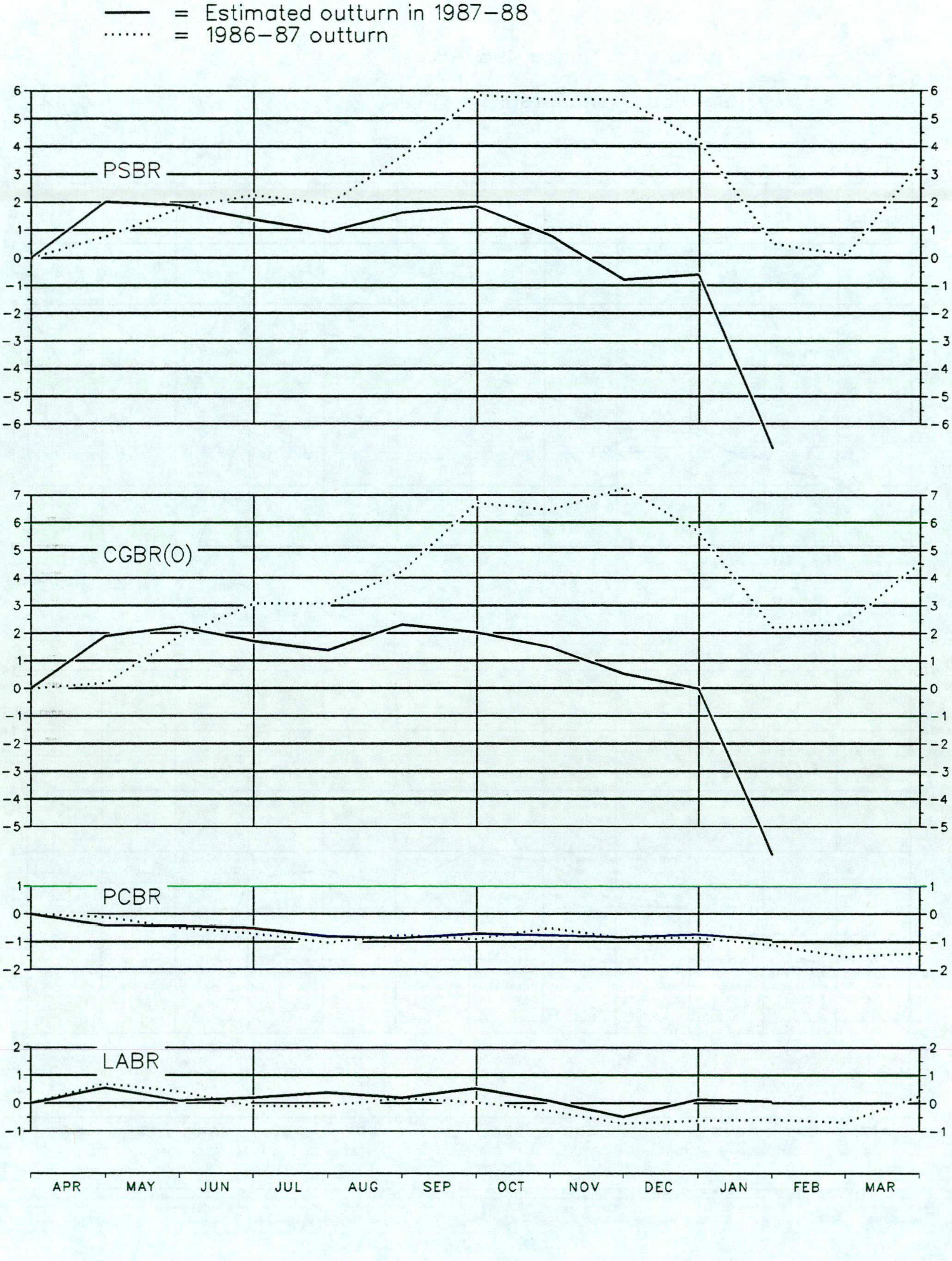
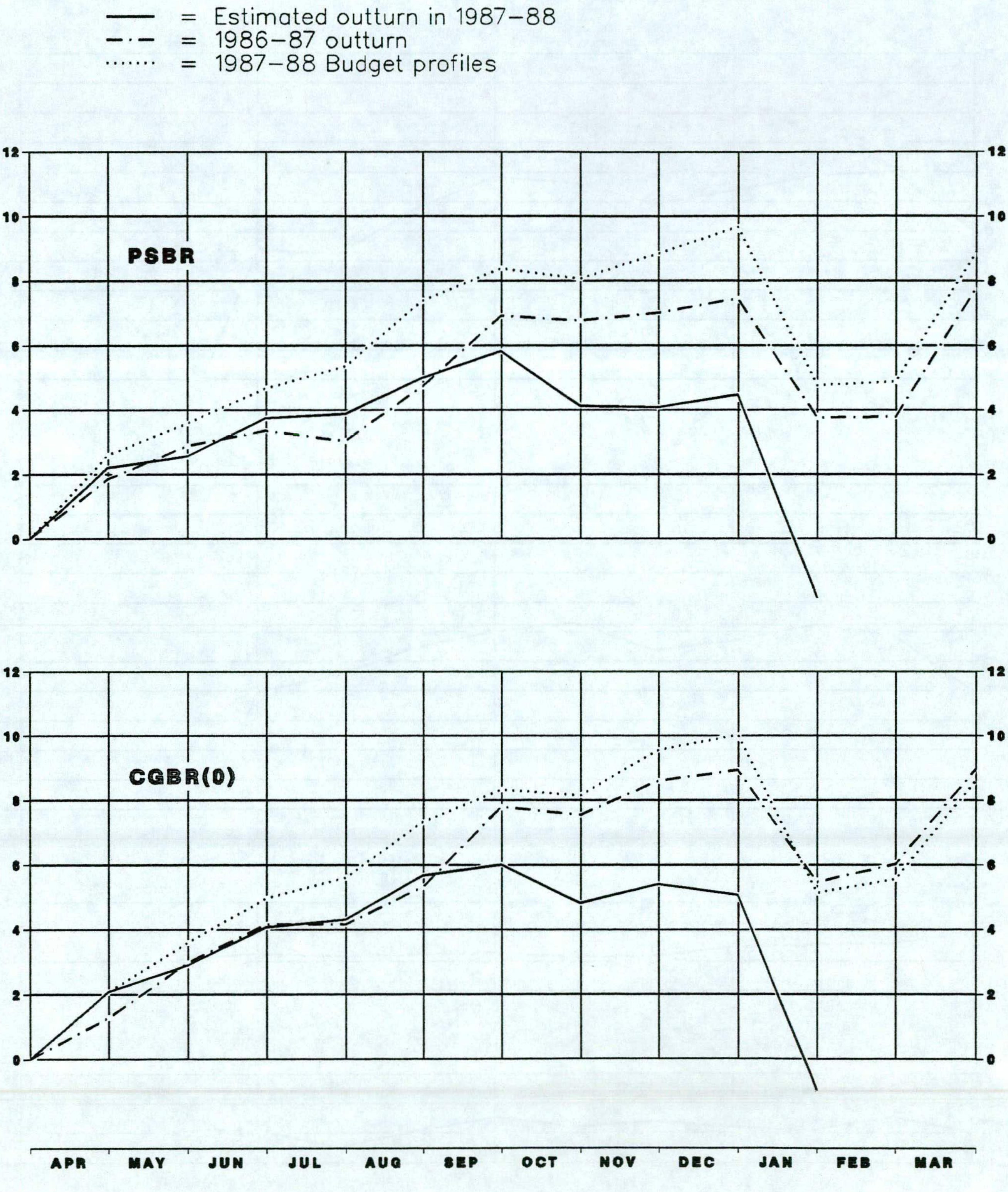


Chart 3: Comparisons excluding privatisation proceeds

£ billion cumulative



Borrowing in January

(Outturn compared with the Treasury's Winter Economic forecast)

1. The provisional estimate of the PSBR in January is a surplus of £6.3 billion. As shown in the table below the provisional outturn was a £0.1 billion higher surplus than the Treasury's Winter Economic forecast, with the LABR coming out at a lower surplus than forecast, more than offset by higher surpluses than forecast on the PCBR and CGBR(O).

Table 1: **January 1988 borrowing requirements**

£ billion

	PSBR	Comprising		
		CGBR(O)	LABR	PCBR
Forecast	-6.2	-5.7	-0.3	-0.1
Outturn	-6.3	-6.0	-0.1	-0.2
Difference	-0.1	-0.3	0.2	-0.1

2. The surplus on central government's own account was £6.0 billion, a £0.3 billion higher surplus than was allowed for in the Treasury's Winter Economic Forecast. Higher national insurance contributions ((by £0.3 billion), lower departmental expenditure (by £0.4 billion) and lower net debt interest (by £0.2 billion) were partly offset by lower Inland Revenue receipts (by £0.7 billion), mainly due to lower receipts of Corporation Tax including Advanced Corporation Tax.

3. The CGBR(O) in January also reflects the final repurchases of BP shares at a cost in January of £15 million. This cost has been netted off the January figure for privatisation proceeds.

4. The Local authorities' borrowing requirement (LABR) in January, a surplus of £0.1 billion, was somewhat lower than in the two previous years, but similar to the average in the 3-4 years prior to that. This lower LABR could be due to partial unwinding of the unusually

high LABR in December.

5. The Public corporations' borrowing requirement (PCBR) in January is provisionally a surplus of £0.2 billion, compared to a forecast surplus of £0.1 billion. The January PCBR is broadly in line with last year's figure but lower than the years before that. The PCBR is compiled in aggregate using information supplied by the banks and central government. The industries make separate monthly returns which give details of their borrowing. The industry returns for January which have been received so far show most industries borrowing less than forecast.

April to January

6. The cumulative PSBR for April to December has been revised down by £0.2 billion mainly due to new information from the DOE quarterly returns. The cumulative PSBR for the first ten months of 1987-88 is £6.7 billion below the Budget profile (see chart 1 and Table 2) and £7.4 billion below the first ten months of 1986-87. Excluding privatisation proceeds the PSBR for April to January is a surplus of £1.8 billion. This is the first time that the cumulative PSBR excluding privatisation proceeds has been a surplus this year. Excluding privatisation proceeds the PSBR so far this year is £6.6 billion below the Budget profile and £5.6 billion lower than the equivalent period last year.

Table 2: Total April-January borrowing requirements

£ billion

	PSBR	Comprising		
		CGBR(O)	LABR	PCBR
Budget forecast	-0.2	0.2	0.1	-0.4
Outturn	-6.9	-6.0	0.1	-0.9
Difference	-6.7	-6.2	-	-0.5

7. In April to January the central government's own account showed cumulatively a surplus of £6.0 billion compared with borrowing of £0.2 billion in the Budget profile. Two thirds of the undershoot is the result of higher receipts and one third the result of lower expenditure. Table 3 shows where differences on individual components have occurred.

Table 3: CGBR(O) April – January: Differences from Budget profile

	£ billion	percentage difference
Receipts		
Inland Revenue	+2.6	+5.0
Customs and Excise	+0.8	+2.2
NICs	+0.4	+1.6
Privatisation proceeds	+0.1	+1.9
Interest and dividends	–	+0.1
Other receipts	+0.3	+10.7
Total receipts	**+4.1**	**+3.3**
Expenditure		
Interest payments	–0.2	–1.7
Departmental expenditure [1]	–1.8	–1.6
Total expenditure	**–2.0**	**–1.6**
Net effect on CGBR(O)	**–6.2**	

[1] on a cash basis, net of certain receipts and on-lending

8. The main factors reducing borrowing are:

- higher Inland Revenue receipts, mainly due to higher Corporation Tax (£0.9 billion), including ACT and North Sea MCT. Income tax is £1.0 billion higher, with higher PAYE partly offset by lower than expected other income tax. PRT and stamp duties are about £0.3 and £0.4 billion respectively higher than forecast at Budget time.

- higher Customs and Excise receipts,mainly due to higher VAT (£0.7 billion) and tobacco duties (£0.2 billion). Higher than expected Keith effects may have contributed £0.2 billion to the higher than expected VAT, but the main explanation is probably higher consumer spending on goods and services subject to VAT – which does not yet appear to have been reflected in the official expenditure figures. Other Customs and Excise duties are slightly lower than forecast at Budget time.

- higher national insurance contributions.

- higher other receipts, about half of which is due to an increase in the balances held on behalf of the European Community.

- A shortfall on departmental expenditure (measured on a cash basis) of about £1.8 billion. This is not fully reflected in expenditure returns by departments (the APEX returns), which show Supply expenditure £1.0 billion below budget profile. However, there are definitional and timing differences between the APEX and cash measurements. On the Apex measure the main programmes which are below profile are defence, overseas aid, employment, social security and grants to British Rail. The main programmes above profile are ECGD's trading account, (due to delays in the re-financing programme), health and payments to British Coal.

9. After taking account of a downward revision of £0.3 billion to the LABR for April to December due to new quarterly information from the DOE returns, the local authority borrowing requirement in April to January is £0.1 billion, as forecast in the Budget profile and £0.6 billion higher than April to January in 1986-87.

10. The cumulative PCBR for the first ten months of 1987-88 is a surplus of £0.9 billion, compared to a Budget forecast surplus of £0.4 billion. Table 4 (see table 3 attached) shows cumulative borrowing to January for the PCBR and selected public corporations, excluding those privatised and reclassified since April 1986. Borrowing estimates for individual corporations are derived from their own returns, and are not fully consistent with the aggregate PCBR estimates. However, the Electricity Council, British Steel, the Post Office, Water and "other" public corporations have all borrowed less than last year and less than was forecast at Budget time.

Table 4: Public Corporations' borrowing April-January

£million (-indicates lower borrowing)

	Difference from 1986-87	Difference from Budget profile+
Coal	-*	-60*
Electricity	-70	-40
British Steel	-250	-220
Post Office	-360*	-360*
Water	-240*	-130*
Other NIs	-280*	20 *
Other PCs	-230*	-230*
PCBR	-1070**	-540**

*No January figure yet available figures cover April- December only

**Excluding industries privatised during 1986-87 and 1987-88

+components do not sum to total difference in PCBR, because of incomplete information on borrowing in December.

Chart 4: Components of central government receipts and expenditure

£ billion

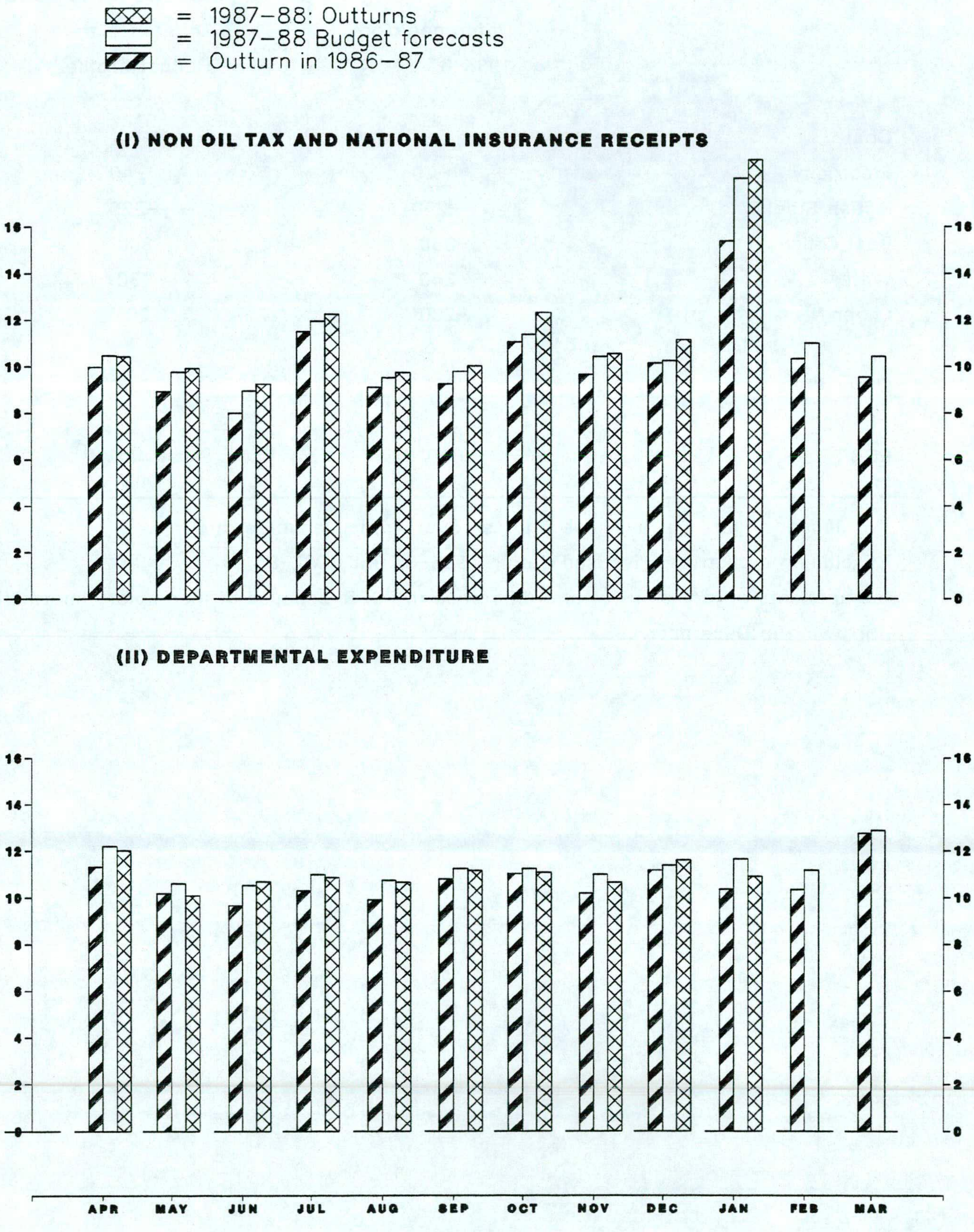


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Table 5: PSBR for 1987-88 - comparisons with 1986-87 and 1987 Budget profile

£ billion

	1986-87	1987-88		Differences from	
	Outturn	Budget profile	Latest update[1]	1986-87 outturn	Budget profile
	1	2	3	3-1	3-2
Apr	0.8	2.4	**2.0**	1.3	-0.4
May	1.0	0.7	**-0.1**	-1.1	-0.8
Jun	0.5	-0.6	**-0.5**	-1.0	0.1
Q2	2.3	2.5	**1.4**	-0.9	-1.1
Jul	-0.3	0.2	**-0.4**	-0.1	-0.6
Aug	1.7	1.6	**0.7**	-1.0	-1.0
Sep	2.2	0.4	**0.2**	-2.0	-0.2
Q3	3.6	2.2	**0.5**	-3.1	-1.7
Oct	-0.2	-1.1	**-1.1**	-0.9	-
Nov	-	0.8	**-1.6**	-1.6	-2.4
Dec	-1.5	0.8	**0.2**	1.7	-0.6
Q4	-1.6	0.5	**-2.5**	-0.8	-3.0
Jan	-3.7	-5.4	**-6.3**	-2.6	-0.9
Cumulative					
Apr	0.8	2.4	**2.0**	1.3	-0.4
May	1.8	3.1	**1.9**	0.1	-1.2
Jun	2.3	2.5	**1.4**	-0.9	-1.1
Jul	1.9	2.7	**0.9**	-1.0	-1.7
Aug	3.6	4.3	**1.6**	-2.0	-2.7
Sep	5.8	4.7	**1.8**	-4.0	-2.8
Oct	5.7	3.6	**0.8**	-4.9	-2.8
Nov	5.7	4.4	**-0.8**	-6.5	-5.2
Dec	4.2	5.2	**-0.6**	-4.8	-5.8
Jan	0.5	-0.2	**-6.9**	-7.4	-6.7

[1]Figures for April - January are outturns

Table 6: Borrowing requirement monthly profiles April–February,1987–88
(Budget profiles in italics for comparison) £ billion

	PSBR		CGBR(O)		LABR		PCBR	
Apr	**2.0**	*2.4*	**1.9**	*1.9*	**0.5**	*0.7*	**-0.4**	*-0.2*
May	**-0.1**	*0.7*	**0.3**	*1.2*	**-0.5**	*-0.2*	**-**	*-0.4*
Jun	**-0.5**	*-0.6*	**-0.5**	*-0.3*	**0.1**	*-0.4*	**-0.1**	*0.1*
Jul	**-0.4**	*0.2*	**-0.3**	*0.1*	**0.2**	*0.2*	**-0.3**	*-0.1*
Aug	**0.7**	*1.6*	**0.9**	*1.3*	**-0.2**	*0.3*	**-0.1**	*-*
Sep	**0.2**	*0.4*	**-0.3**	*0.4*	**0.3**	*-0.1*	**0.2**	*0.1*
Oct	**-1.1**	*-1.1*	**-0.5**	*-1.0*	**-0.5**	*-0.3*	**-0.1**	*0.2*
Nov	**-1.6**	*0.8*	**-1.0**	*1.4*	**-0.6**	*-0.5*	**-0.1**	*-0.2*
Dec	**0.2**	*0.8*	**-0.5**	*0.5*	**0.6**	*0.2*	**0.1**	*0.1*
Jan	**-6.3**	*-5.4*	**-6.0**	*-5.4*	**-0.1**	*0.1*	**-0.2**	*-0.1*
Cumulative								
Apr	**2.0**	*2.4*	**1.9**	*1.9*	**0.5**	*0.7*	**-0.4**	*-0.2*
May	**1.9**	*3.1*	**2.2**	*3.1*	**0.1**	*0.6*	**-0.4**	*-0.6*
Jun	**1.4**	*2.5*	**1.7**	*2.8*	**0.2**	*0.1*	**-0.5**	*-0.4*
Jul	**0.9**	*2.7*	**1.4**	*2.9*	**0.4**	*0.3*	**-0.8**	*-0.6*
Aug	**1.6**	*4.3*	**2.3**	*4.2*	**0.2**	*0.6*	**-0.9**	*-0.6*
Sep	**1.8**	*4.7*	**2.0**	*4.6*	**0.5**	*0.5*	**-0.7**	*-0.5*
Oct	**0.8**	*3.6*	**1.5**	*3.7*	**0.1**	*0.2*	**-0.8**	*-0.3*
Nov	**-0.8**	*4.4*	**0.5**	*5.1*	**-0.5**	*-0.2*	**-0.8**	*-0.5*
Dec	**-0.6**	*5.2*	**-**	*5.5*	**0.1**	*-*	**-0.7**	*-0.4*
Jan	**-6.9**	*-0.2*	**-6.0**	*0.2*	**0.1**	*0.1*	**-0.9**	*-0.4*

	Excluding privatisation proceeds PSBR		CGBR(O)		Memo item: privatisation proceeds	
Apr	**2.2**	*2.6*	**2.1**	*2.1*	**0.2**	*0.2*
May	**0.4**	*1.0*	**0.8**	*1.5*	**0.5**	*0.3*
Jun	**1.2**	*1.1*	**1.2**	*1.4*	**1.7**	*1.7*
Jul	**0.1**	*0.7*	**0.2**	*0.6*	**0.6**	*0.5*
Aug	**1.1**	*2.0*	**1.4**	*1.7*	**0.4**	*0.4*
Sep	**0.8**	*1.0*	**0.3**	*1.0*	**0.6**	*0.6*
Oct	**-1.7**	*-0.3*	**-1.2**	*-0.2*	**-0.6**	*0.8*
Nov	**-**	*0.8*	**0.6**	*1.4*	**1.5**	*-*
Dec	**0.4**	*0.8*	**-0.3**	*0.5*	**0.2**	*-*
Jan	**-6.3**	*-4.9*	**-6.0**	*-4.9*	**-**	*0.5*
Cumulative						
Apr	**2.2**	*2.6*	**2.1**	*2.1*	**0.2**	*0.2*
May	**2.6**	*3.6*	**2.9**	*3.6*	**0.7**	*0.5*
Jun	**3.8**	*4.7*	**4.1**	*5.0*	**2.4**	*2.2*
Jul	**3.9**	*5.4*	**4.3**	*5.6*	**2.9**	*2.7*
Aug	**5.0**	*7.4*	**5.7**	*7.3*	**3.4**	*3.1*
Sep	**5.8**	*8.4*	**6.0**	*8.3*	**4.0**	*3.7*
Oct	**4.1**	*8.1*	**4.8**	*8.2*	**3.3**	*4.5*
Nov	**4.1**	*8.9*	**5.4**	*9.6*	**4.9**	*4.5*
Dec	**4.5**	*9.7*	**5.1**	*10.0*	**5.1**	*4.5*
Jan	**-1.8**	*4.8*	**-1.0**	*5.1*	**5.1**	*5.0*

110/4 sn 3783/35

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TABLE 7

CENTRAL GOVERNMENT TRANSACTIONS - JANUARY OUTTURN

£ billion

	January		
	Forecast	**Outturn**	**Difference**
Receipts			
Inland Revenue	12.8	12.0	-0.7
Customs and Excise	3.8	3.9	0.1
National Insurance Contributions	2.5	2.8	0.3
Privatisation proceeds	-0.1	-	0.1
Interest and dividends	0.4	0.5	0.1
Other receipts	-0.4	-0.3	0.1
Total Receipts	19.1	18.9	-0.2
Expenditure			
Interest payments	2.1	2.0	-0.1
Departmental expenditure (a)	11.3	10.9	-0.4
Total expenditure	13.4	12.9	-0.5
CGBR(O)	-5.7	-6.0	-0.3
CGBR(O) excluding privatisation proceeds	-5.8	-6.0	-0.2
On-lending to LAs	0.1	-	-0.1
On-lending to PCs	0.1	0.1	-
CGBR	-5.5	-5.9	-0.4

(a) on a cash basis, net of certain receipts

+ = higher receipts, and higher borrowing, higher expenditure
- = lower receipts, and lower borrowing, lower expenditure

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TABLE 8

CENTRAL GOVERNMENT TRANSACTIONS - CUMULATIVE
DIFFERENCES FROM BUDGET PROFILES

£ billion

	Difference in outturn April-January	
	£ billion	Percentage difference
Receipts		
Inland Revenue	2.6	5.0
Customs and Excise	0.8	2.2
National Insurance Contributions	0.4	1.6
Privatisation proceeds	0.1	1.9
Interest and dividends	-	0.1
Other receipts	0.3	10.7
Total Receipts	4.1	3.3
Expenditure		
Interest payments	-0.2	1.7
Departmental expenditure (a)	-1.8	-1.6
Total expenditure	-2.0	-1.6
CGBR(O)	-6.2	..
CGBR(O) excluding privatisation proceeds	-6.1	..
On-lending to LAs	1.7	..
On-lending to PCs	-0.2	..
CGBR	-4.8	..

(a) on a cash basis, net of certain receipts

+ = higher receipts, and higher borrowing, higher expenditure
- = lower receipts, and lower borrowing, lower expenditure

TABLE 9:

CONSOLIDATED FUND REVENUES - % changes on year earlier

	FORECAST FOR 1987-88		**APRIL 1987-JANUARY 1988**			
	(i) **FSBR(a)**		(ii) **FSBR**		(iii) **Outturn**	
1. Total Inland Revenue	7		7		12½	
of which: Income Tax		3½		4		7
Corporation Tax (d)		20½		21		28
North Sea taxes (c)		-16½		-18½		-6
Other (Stamp Duties and Capital Taxes)		13½		14		25½
2. Customs and Excise	6½		6		8½	
of which: VAT		9		8½		12½
Specific Duties		3		3		3½
Other (e)		7½		6½		7½
3. Vehicle Excise Duty	-½		5		3	
4. Asset Sales	14		53		56	
5. Other Consolidated Fund Revenue*	-16		-17½		3½	
6. Timing Adjustment (f)	64½		-100		79½	
7. **TOTAL CONSOLIDATED FUND REVENUE**	5½		7		11½	
Memorandum Items:						
Non North Sea Taxes		7		7½		11
North Sea Oil Taxes and Royalties		-13½		-15		-3½

* This includes oil royalties, EC refunds, coinage receipts and CFERs.

(a) using 1986-87 outturn as a base
(b) using 1986-87 outturn as a base
(c) Payments of PRT, advance PRT and North Sea corporation tax but excluding royalties
(d) Includes onshore and North Sea ACT
(e) Includes difference between receipts and payments to Consolidated Fund for April to January
(f) Reflects privatisation proceeds paid initially to Paymaster General and then to Consolidated Fund

From: ALLEN RITCHIE
16 February 1988

MR R.I.G. ALLEN - IDT

MR LANG - CSO Press Office

cc List A

Chancellor
Chief Secretary
Financial Secretary
Paymaster General
Economic Secretary
Sir P Middleton
Sir T Burns
Mr Anson
Mr Monck
Mr Scholar
Mr Peretz
Mr Sedgwick
Mrs Butler
Mr Grice

Mr Mowl
Miss O'Mara
Mr Pickford
Mr Bush
Mr Franklin
Mrs Todd
Mr R Evans
Miss Chapman
Mr Mansell - CSO
Mr Richardson - CSO
Mr Wright B/E
Mr Gray - No 10

List B
(distributed at 11.30am, 16 February)

Mr C.M. Kelly
Mr Cropper
Mr Tyrie
Mr Call
Mr Ko - IR
Mr Balley - C and E

BRIEFING FOR 16 FEBRUARY PSBR PRESS NOTICE

The PSBR figures for January will be published at 11.30am on 16 February. The provisional outturns, together with figures for the first ten months of 1986-87 and 1987-88, are shown in Table 1. Cumulative figures for the PSBR and its components for 1985-86 and 1986-87 are shown in Table 2 overleaf. Table 3 shows outturns excluding privatisation proceeds.

Table 1: **Borrowing requirement outturns**

£ billion

	Apr 1986 -Jan 1987	Apr 1987 -Jan 1988	Jan 1988
Central government on own account	2.2	-6.0	**-6.0**
Local authorities	-0.6	0.1	**-0.1**
Public corporations	-1.1	-0.9	**-0.2**
PSBR	0.5	-6.9	**-6.3**
Memo: PSBR (excluding privatisation proceeds)	3.8	-1.8	-6.3

Note: Figures may not sum precisely because of rounding.

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(until 11.30am 16 February 1988)

Table 2: PUBLIC SECTOR BORROWING REQUIREMENT – Comparison with the last two years

Cumulative £ billion

	Central government on own account			Local authorities borrowing requirement			Public corporations borrowing requirement			Public sector borrowing requirement		
	1985-86	1986-87	1987-88	1985-86	1986-87	1987-88	1985-86	1986-87	1987-88	1985-86	1986-87	1987-88
Apr	1.1	0.2	**1.9**	0.8	0.7	**0.5**	−0.2	−0.1	**−0.4**	1.8	0.8	**2.0**
May	2.3	1.9	**2.2**	0.8	0.4	**0.1**	−0.4	−0.5	**−0.4**	2.7	1.8	**1.9**
Jun	2.7	3.1	**1.7**	0.5	−0.1	**0.2**	−0.5	−0.7	**−0.5**	2.6	2.3	**1.4**
Jul	3.6	3.1	**1.4**	0.8	−0.1	**0.4**	−1.2	−1.0	**−0.8**	3.1	1.9	**0.9**
Aug	4.6	4.2	**2.3**	0.9	0.2	**0.2**	−1.2	−0.8	**−0.9**	4.3	3.6	**1.6**
Sep	5.1	6.7	**2.0**	1.1	0.0	**0.5**	−0.7	−0.9	**−0.7**	5.6	5.8	**1.8**
Oct	5.0	6.5	**1.5**	0.7	−0.3	**0.1**	−0.5	−0.5	**−0.8**	5.3	5.7	**0.8**
Nov	6.2	7.3	**0.5**	0.1	−0.7	**−0.5**	−0.3	−0.9	**−0.8**	6.0	5.7	**−0.8**
Dec	7.4	5.7	**−0.0**	0.4	−0.6	**0.1**	−0.2	−0.9	**−0.7**	7.6	4.2	**−0.6**
Jan	2.9	2.2	**−6.0**	0.5	−0.6	**0.1**	−0.2	−1.1	**−0.9**	3.2	0.5	**−6.9**
Feb	2.9	2.3		0.4	−0.7		−0.6	−1.5		2.8	0.1	
Mar	4.3	4.5		1.7	0.2		−0.2	−1.4		5.8	3.4	

Note: Figures may not sum precisely because of rounding.

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(until 11.30am 16 February 1988)

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(until 11.30am 16 February 1988)

Table 3: PUBLIC SECTOR BORROWING REQUIREMENT EXCLUDING PRIVATISATION PROCEEDS

Cumulative £ billion

	Central government on own account			Local authorities borrowing requirement			Public corporations borrowing requirement			Public sector borrowing requirement		
	1985-86	1986-87	1987-88	1985-86	1986-87	1987-88	1985-86	1986-87	1987-88	1985-86	1986-87	1987-88
Apr	1.1	1.3	**2.1**	0.8	0.7	**0.5**	-0.2	-0.1	**-0.4**	1.8	1.9	**2.2**
May	2.5	3.0	**2.9**	0.8	0.4	**0.1**	-0.4	-0.5	**-0.4**	2.9	2.9	**2.6**
Jun	4.0	4.2	**4.1**	0.5	-0.1	**0.2**	-0.5	-0.7	**-0.5**	3.9	3.4	**3.8**
Jul	5.0	4.2	**4.3**	0.8	-0.1	**0.4**	-1.2	-1.0	**-0.8**	4.5	3.0	**3.9**
Aug	6.2	5.3	**5.7**	0.9	0.2	**0.2**	-1.2	-0.8	**-0.9**	5.9	4.7	**5.0**
Sep	6.8	7.8	**6.0**	1.1	0.0	**0.5**	-0.7	-0.9	**-0.7**	7.3	6.9	**5.8**
Oct	6.7	7.5	**4.8**	0.7	-0.3	**0.1**	-0.5	-0.5	**-0.8**	7.0	6.8	**4.1**
Nov	8.2	8.6	**5.4**	0.1	-0.7	**-0.5**	-0.3	-0.9	**-0.8**	7.9	7.0	**4.1**
Dec	9.7	8.9	**5.1**	0.4	-0.6	**0.1**	-0.2	-0.9	**-0.7**	9.9	7.5	**4.5**
Jan	5.1	5.5	**-1.0**	0.5	-0.6	**0.1**	-0.2	-1.1	**-0.9**	5.4	3.8	**-1.8**
Feb	5.2	6.0		0.4	-0.7		-0.6	-1.5		5.1	3.8	
Mar	7.0	9.0		1.7	0.2		-0.2	-1.4		8.5	7.8	

Note: Figures may not sum precisely because of rounding.

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(until 11.30am 16 February 1988)

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(Until 11.30am 16 February 1988)

SUMMARY OF LINE TO TAKE

PSBR in January provisionally a surplus of £6.3 billion. Excluding privatisation proceeds, PSBR for first 10 months of 1987-88 was a surplus of £1.8 billion, as compared with borrowing of £3.8 billion in same period of 1986-87.

1. January PSBR

Background

City forecasts of January are for a surplus in a range from £4 billion to £5¼ billion. Average is a surplus of £4.4 billion.

Line to take

January PSBR always a surplus - main month for mainstream corporation tax. CT receipts for January provisionally totalled around £6 billion (1986-87 - just under £5 billion).

2. PSBR, April-January

Line to take

Excluding privatisation proceeds, PSBR in first 10 months of 1987-88 was a surplus of £1.8 billion, as compared with borrowing of £3.8 billion in 1986-87. Local authorities borrowing, however, running at level higher than last year (see Q.11).

3. PSBR undershoot on Autumn Statement forecast for 1987-88?

Background

Forecast for 1987-88 revised in Autumn Statement to £1 billion, (£3 billion lower than forecast at Budget time). City commentators have said that this is still an over forecast and that PSBR likely to be in surplus for 1987-88.

Line to take

Autumn Statement forecast now looking likely to be undershot. But still major uncertainties about the eventual outcome. Main uncertainties are size of end year surge in central government expenditure and local authorities' borrowing. New forecast in Budget.

4. Privatisation proceeds in 1987-88

Background

Privatisation proceeds so far this year £5.1 billion, compared with £3.3 billion in same period last year. Autumn Statement figure for 1987-88 as a whole £5 billion, unchanged from FSBR forecast. Costs of privatisations offset the gross privatisation proceeds, so quite feasible that total for year as whole could be slightly lower than cumulative total to end-January. No further instalments from earlier privatisations scheduled for the remainder of 1987-88.

Line to take

Net privatisation proceeds in January were close to zero.

5. Effect on PSBR of BP share support scheme

Background

BP share support scheme closed on 6 January. Treasury press notice on 7 January said that cost of Issue Department purchases of BP shares was around £27 million (around 39 million shares at 70p each). Purchases in January - counted in January PSBR - around £15 million.

Line to take

Negligible effect on PSBR.

6. Consolidated Fund Revenues

Background

Press notice shows that Consolidated Fund (CF) revenues in first ten months of 1987-88 were 11½ per cent higher than in the same period last year, comprising 12½ per cent increase in Inland Revenue receipts, 8½ per cent increase in Customs and Excise receipts, and 19 per cent in "other revenues". "Other revenues" include privatisation proceeds when they are transferred into Consolidated Fund - these amounts may differ from total privatisation proceeds given in table 5 of press notice. Proceeds received by HMG are usually transferred to Consolidated Fund with a lag.

No forecast of Consolidated Fund revenue given in Autumn Statement, but total taxes on income, expenditure and capital in 1987-88 forecast to be £2.3 billion higher than in FSBR. These were forecast in the Autumn Statement to increase by 8¾ per cent compared with 7 per cent in the FSBR. See Autumn Statement para 1.57 for composition of additional receipts.

Line to take

Consolidated Fund revenues in April to January £103.5 billion, 11½ per cent up on same period last year. Includes some privatisation proceeds. Excluding privatisation proceeds revenues up by 10 per cent.

7. Inland Revenue Receipts

Background

Inland Revenue receipts in January £12.0 billion. Total for April-January £54.7 billion, (12½ per cent up on same period last year). FSBR forecast for year as whole was a rise of 7½ per cent on 1986-87. More detailed monthly figures will be published later in Financial Statistics, Table 3.13. No forecast of total Inland Revenue receipts given in Autumn Statement, but stated that North Sea revenues £0.6 billion higher, income tax about £½ billion higher and Corporation tax about £¾ billion higher than in FSBR.

Line to take

Receipts in April-January £54.7 billion, 12½ per cent up on same period last year. January receipts include around £6 billion corporation tax (provisional estimate) (1986-87 - just under £5 billion).

8. Customs and Excise Receipts

Background

Customs and Excise receipts in January £3.9 billion. Total for April-January £37.0 billion (8½ per cent up on same period last year). FSBR forecast for year as whole was a rise of 6½ per cent on 1986-87. More detailed monthly figures will be published later in Financial Statistics, Table 3.14. No forecast for Customs and Excise receipts given in Autumn Statement, but stated that VAT about £½ billion higher than in Budget forecast.

Line to take

Receipts in April-January £37.0 billion, 8½ per cent up on same period last year.

9. Supply Expenditure

Background

FSBR gave a figure for provision for supply in 1987-88 but not a forecast of outturn because public expenditure Reserve was not allocated to individual components of expenditure, (but public expenditure total used in PSBR forecast assumed that the Reserve was fully spent).

Line to take

Provisional outturn for supply expenditure in January £8.8 billion. Total April-January 1987-88 (provisional £85.8 billion) up 3½ per cent on same period last year. Excluding advance contributions to EC Budget paid from supply in 1986-87, increase is 4½ per cent.

10. Central Government Borrowing

Background

CG own account borrowing in January, surplus of £6.0 billion. Total for April-January, a surplus of £6.0 billion (1986-87, borrowing of £2.2 billion). Privatisation proceeds, April-January, £5.1 billion (1986-87, £3.3 billion).

Line to take

Excluding privatisation proceeds, CG own account borrowing over April to January lower by £6½ billion than same period last year.

11. Local Authorities

Background

LABR (provisionally) a surplus of £0.1 billion in January (zero borrowing in January 1987). Local authorities recorded borrowing of £0.1 billion during first ten months of 1987-88. (Surplus of £0.6 billion for same period in 1986-87). Some revisions to earlier months - see Q.13.

Line to take

LABR for first 10 months of 1987-88 around £¾ billion higher than for same period in previous year.

12. Public Corporations

Background

PCBR (provisionally) a surplus of £0.2 billion in January. Surplus of £0.9 billion over April to January. (Surplus of £1.1 billion, April-January, 1986-87, but aggregate then included BGC, for most of year, and BA).

Line to take

PCBR so far in 1987-88 little different from last year.

Revisions to last month's estimates

Background

PSBR for April-November revised upwards last month by £0.4 billion. Main factor - upward revision of £0.5 billion to LABR, reflecting revisions to data on LA short-term financial assets. Further revisions this month on same account, plus usual three-monthly revisions on receipt of full quarterly information. This month's revisions partly reverse last month's.

Line to take

PSBR for April to December revised downwards by £0.2 billion since last month. LABR revised down by £0.3 billion and PCBR revised up by £0.1 billion. Revisions reflect incorporation of full quarterly information for Q4 on LA and PC borrowing, and changes to data on LA short-term financial assets.

Allen Ritchie (270-5029)
PSF Division, HM Treasury

002/2989

prup

FROM: JILL RUTTER
DATE: 24 February 1988

PRINCIPAL PRIVATE SECRETARY

PPS

cc:
PS/Financial Secretary
PS/Paymaster General
PS/Economic Secretary
Sir Peter Middleton
Mr Anson
Mr Phillips
Miss Peirson
Mr C W Kelly
MrTurnbull
Mr Saunders
Mrs M Brown
Mr Gilhooly
Mr Gieve
Mr Mortimer
Mr Pickford
Mr R I G Allen
Mr Bush
Mr Cropper
Mr Call
Mr Tyrie

CHIEF SECRETARY'S SPEECH IN PEWP DEBATE

I attach the final version of the Chief Secretary's speech, which reflects the comments the Chancellor made on the version I sent you last night, as well as comments from No. 10 and DHSS on the section on nurses' pay. If there are any further comments, could I have them as soon as possible.

2 The peroration is likely to be changed substantially when the Chief Secretary speaks.

Jill Rutter

JILL RUTTER
Private Secretary

CHIEF SECRETARY'S SPEECH
PUBLIC EXPENDITURE WHITE PAPER DEBATE
ON WEDNESDAY, 24 FEBRUARY

The broad lines of policy on public expenditure were announced last November in the Autumn Statement and were debated last month. That debate enabled the House to consider the trends in public expenditure and the way in which priorities had changed between programmes.

2 The Public Expenditure White paper before us today builds on that and provides a more comprehensive account of

- what Government is spending
- the service it is delivering

and its efforts to secure greater value for money.

3 What the White Paper does not provide is a new statement of policy. I suspect that was not fully understood last month when many people affected to be disappointed that it did not contain fresh expenditure plans. Frankly, it would have been extra-ordinary if it *had* done so only weeks after our plans were announced in the Autumn Statement.

4 The Public Finance cycle is quite clear. It begins with the Budget and the MTFS in the Spring . That sets out our taxation and borrowing policies. It continues with the Public Expenditure Survey to determine future spending plans. These are set out in broad terms in the Autumn Statement. It concludes with the Public Expenditure White Paper, followed by this debate which provides an opportunity to consider the Government's management of the taxpayers money. We are helped in this by the report from the Treasury and Civil Service Committee which makes a number of interesting observations and recommendations. The Government will respond to these as soon as possible and I shall refer to a number of them shortly.

5 It is crystal clear that the strength of the public finances has created the conditions for a sound economy, and the soundness of the economy has fed back to the public finances. The crisis so lovingly predicted by RHG Sparkbrook has failed to arrive yet again. Like Bunter's Postal Order it is forever in the post. Rising real incomes and corporate profits boost the revenue side of the account. But a growing economy brings benefits for expenditure as well. Nationalised industries are producing better results: for example, the rising profits at British Steel and increasing passenger revenues of British Rail. Falling unemployment is reducing the growth of social security spending; a boyuant economy is enabling central Government, local authorities and new towns to step up their disposals of surplus assets. These are changes few would have predicted a few years ago.

6 The lower borrowing that has resulted from these changes is reducing the costs of servicing the national debt. Debt interest has now fallen from its peak of 5¼ per cent of GDP in 1981-82 to around 4¼ per cent this year. We expect this to fall still further and this will enable us to spend more on priority programmes. Let me put this in context. If the PSBR had remained at its 1978-79 share of GDP, cumulative borrowing would by now be around £80 billion higher with increased debt servicing costs of over £8 billion a year. That would be the equivalent of an extra 7p on the standard rate of income tax just to finance the debt. None of that extra revenue would have gone on Education or Social Security or Health. It would all have gone to our creditors. That would be the result of the policies the Opposition still cling to with such hide-bound affection.

7 We are in the fortunate position that we have dumped these policies. That is why our economic performance is so strong, but it will only stay that way if we continue with the policies which got us to this point in the first place. We propose to do that.

8 In the Survey of public spending conducted last year, we added £4½ billion to the planned programme expenditure in 1988-89 and £6 billion in 1989-90 thanks to a growing economy, still reducing public spending as a proportion of national income.

9 That proportion has already fallen from 43 per cent when we took office to 42 per cent now - down over 4 per cent from its peak in 1982-83. But that has not meant cuts - because national income has risen by 19 per cent. That proportion is set to fall further - to 41 per cent by 1990-91. But that further fall does not mean "cuts" either. This is all in stark contrast with the rising share of national income absorbed each year by public spending in the 1960s and 1970s.

10 The plans contained in this White Paper show that within the constraint we have set ourselves, we have been able to strengthen priority services such as health, law and order, education, defence and inner cities.

11 In their report, the Select Committee have raised some genuine issues which need to be addressed on the health service and I shall respond to these. But let me first put the position in context. Measured in all sorts of ways, the NHS is expanding, improving and becoming more efficient, as the programme of cost improvements has clearly demonstrated.

- indicators of health show significant improvements in life expectancy in recent years and large reductions in deaths from a wide range of conditions;

- indicators of the number of treatments show large increases in patients treated, whether as in-patients, day-patients or out-patients. Since 1978 the output of the hospitals service has increased by over 20 per cent or about 2½ per cent a year;

- and treatments are now being widely offered that barely existed a decade ago.

12 Little of this would have occurred if the Government had not provided increasing resources. But

we have. Total spending on the health service has risen by 32 per cent more than inflation. It has risen too as a proportion of public spending and will continue to do so. It has risen as a proportion of national income. And gross capital spending, - cut so savagely by the Opposition when in Government - has increased by 42 per cent in real terms helped partly by rising capital receipts.

13 In the crucial HCHS sector of the NHS, current expenditure will have increased in 1987-88 by around 10 per cent, well over twice the rate of inflation in the economy generally, and faster than any measure of rising prices in the health sector specifically. If one allows for this and also for the benefit of the cost improvement programme, "the margin available for service development" will have increased by nearly 3 per cent, comfortably ahead of even the most pessimistic estimate of demographic pressures. It rapidly becomes self evident that current difficulties faced in the health service are not simply questions of funding. And funding alone will not solve them.

14 The Government has recognised that there are important issues to be examined. We must consider whether there are other ways of delivering health care which meet people's expectations. In doing so we propose to preserve the principle that a high standard of health care must be available for all regardless of means. That principle is not at risk.

15 That is why we have set in hand a fundamental review of the management and funding of health care in this country.

16 But as well as these fundamental issues the Select Committee was particularly concerned at the uncertainty faced by Health Authorities who have to plan their budgets before the Review Body recommendations are finalised and before consequent decisions on funding are known.

17 I sympathise with this concern and with the dilemma facing Health Authorities. The Government have examined this problem to see if there is a way of resolving it without abdicating responsibility for the control of public expenditure. We are not prepared to commit ourselves in advance to accepting Review Body recommendations unreservedly or to funding resulting awards in full. Nor would any Government. Those decisions can only be made when the recommendations have been studied.

18 However, what we can and will do is remove this uncertainty for Health Authorities in the future. We have decided in future years to bring forward the time-table for the Review Body reports so that decisions can be made on them well before the beginning of the financial year. We hope Review Bodies will be able to submit their reports in time for decisions on them by the end of January or, at the latest, by mid-February.

19 This new timetable will affect the Reports of all the Review Bodies - the Nurses and Midwives Pay Review Body, the Doctors and Dentists Pay Review Body, the Armed Forces Pay Review Body and the Top Salaries Review Body. It will mean, in particular, that the outcome of salary awards will be known to health service treasurers before they finalise their budgets for the coming year. I hope and believe this will remove a great deal of uncertainty for them.

20 We cannot, at this late stage, bring this year's reports on to this timetable but we do propose to try and minimise the period of uncertainty. In particular, it would be difficult to press the Review Body for Nurses to hasten its Report because this year, as the House knows, it is considering a number of important and complex issues including a new clinical grading structure. This seeks to reward skill and responsibility and to give better pay and career prospects to those nurses who choose to stay in areas of direct patient care. This meets precisely the point that so many health service professionals have drawn attention to in recent weeks. The Review Body will also be looking at special pay differentials needed to cope with localised recruitment difficulties.

21 But, as I have said, we do want to minimise the period of uncertainty. Yesterday, my RHF the Prime Minister reminded the House that last year the Government received all the reports of the Review Bodies between 1 and 14 April and announced all decisions, on implementation and on funding, by 23 April. She stressed that if, as we expect, the Reports come in at a similar time this year, the Government will, for its part, be equally expeditious in announcing its decisions. We hope therefore to be in a position to announce decisions no later than the end of April.

22 In short, the position is:

- first, we are carrying out a fundamental review of the management and financing of health care.

- secondly, the timetable for the Review Body reports will, in future years, be brought forward so that the Government can announce its decisions before health authorities finalise their budgets;

- thirdly, we hope that this year we will be able to announce our decisions on the Review Body recommendations and the financing of them no later than the end of April;

23 Decisions on Review Body pay in the Health Service are therefore, only a matter of weeks away. As I have indicated we hope to be in a position to announce our decisions by the end of the first month of the financial year. It would be premature and unacceptable, therefore, to put into effect service reductions on the grounds of uncertainty. Moreover the three concerns of nurses, over the level of their pay, the structure of their pay and over their career prospects, are all being comprehensively and speedily addressed.

24 In the light of these assurances there is one further point I wish to add. In recent weeks only a very small minority of nurses have decided to take part in industrial action. I hope that minority will now realise that the strikes in the health service are unnecessary and damaging to the very service they purport to advance. If they continue, I believe that both public and patients will draw the conclusion that the motives of such action cannot lie in genuine concern over the health service or the pay and conditions of those who work within it.

25 But if such action does continue it will not influence the Government. We will proceed as I have

described today and I reiterate the message I first gave when the White Paper was published - there will be no public expenditure package in the Budget.

26 In their Report, the TCSC drew attention to a number of other points to which I wish briefly to refer. They recognised that the Autumn Statement is now the vehicle for announcing the main results of the Survey and that as a result, the White Paper has, to some extent, been upstaged. The Committee's suggestion that much of the material from Volume I be incorporated into the Autumn Statement is attractive and has a great deal to commend it. We will consider that very carefully and sympathetically despite the obvious technical problems that would need to be overcome.

27 The Committee also suggested that Volume II - now over 400 pages - should be sold as separate departmental booklets, as the Estimates are now. We will consider this proposal sympathetically, along with the corresponding proposals which were made by the Public Accounts Committee last year.

28 I sense that opinion is running in favour of change. The Treasury is already investigating a number of possibilities, and as soon as this work is complete we will put proposals to Parliament.

29 But if we change the way information is reported, there will be consequences for the way it is debated. One possibility, would be for the broad lines of expenditure policy to be debated as part of the Autumn Statement; for Select Committees to consider the departmental booklets and for one or more of their reports to be chosen for debate in May or June. All this will need further consideration.

30 The TCSC invited me in their report to set out the public expenditure effect of the agreement that has been reached on the future financing of the European Community.

31 This agreement concludes a far-reaching review of the Community's finances and policies. It provides effective and legally binding controls on spending, effective measures to reduce agricultural surpluses, and the preservation of the UK's abatement as agreed at Fontainebleau. And no oils and fats tax .

32 Insofar as domestic public expenditure is concerned, the agreement is likely to increase our net payments to Community institutions by some £200-300 million a year. This is compared with what would have happened with a continuation of the 1.4 per cent VAT ceiling, the assumption in the public expenditure White Paper.

Compared with the effective level of spending in 1987, which was already in excess of the 1.4 per cent VAT ceiling, the increase will be some £100-200 million a year.

33 The extra expenditure will be met entirely from the reserve and will not involve reductions in agreed domestic programmes.

34 The timing of the future financing agreement means that the 1988 Community Budget will not be adopted before the end of the current [1987-88] financial year, so the Community's emergency financing arrangements, known as provisional twelfths, will continue into 1988-89 rather than end in 1987-88 as assumed in the White Paper. This will increase our net payments to the Community in 1987-88 by about £240 million, mainly because our abatement in the first three months of 1988 is being made at the rate of the 1987 not the 1988 budget. Once the 1988 budget has been adopted, however, perhaps in May, we shall benefit from a much higher abatement, and the increased abatement will be backdated to the beginning of January. This will reduce our net payments in 1988-89 compared to the figure in the White Paper by the same amount as the increase in 1987-88, around £240 million.

35 Thus in 1988-89 itself, the effect of the future financing package on our net payments will be very broadly offset by the effect of the delay in the adoption of the 1988 budget.

PERORATION

I am acutely aware that the breadth of public expenditure is such that I have not been able to mention many important matters:

- I have not had time to mention the extra £240 million a year we have added to the plans for spending on science and technology.

- Nor the £1½ billion addition to our plans for capital expenditure in each of the next 2 years.

- Nor yet the extra £630 million we are providing for education; £270 million more after taking account of the amounts allowed for teachers' pay and academic restructuring.

- And nor the extra resources we are devoting to the inner cities - and the increased resources we are attracting <u>into</u> the inner cities through creating a partnership with the private sector.

I suspect that these increases will not find a place in the speech we are about to hear from the hon. Member for Dunfermline East either.

36 These public expenditure increases have only been made possible by the sound state of the public finances and the healthy state of the economy. Prudent control of public expenditure has been and will continue to be the cornerstone of the virtuous circle of improving

public finances and a strengthening economy. The complete and abject failure of the Opposition to understand these simple truths will again be in evidence today. They seem to view the hard-won progress of recent years as a kind of windfall, just as I suppose they imagine that the economic failure which toppled them was bad luck. If they don't understand, then the public do - as they have shown very clearly on three memorable occasions.

37 The Opposition will again talk of cuts where there have been increases. They will again air their obsession with pounds spent rather than outputs achieved and this despite the awful illustration of the ILEA that spends more and achieves less than any other education authority in the country.

38 Mr Speaker, all these points they will make are as familiar as they are flawed. The public are not fooled and I trust that this House will not be fooled. I beg to move.

SECRET

CHIEF SECRETARY TO THE TREASURY

CHANCELLOR

PES: HEALTH

You are seeing John Moore this afternoon to discuss the Health programme. He is looking for additions to the programme of £m 738/960/1427. My offer is £m 554/544/880. So ostensibly, the gap between us is £m 184/416/547 (Annex A sets out details). In reality, we should be prepared to accept £m 660/760/1170 (the forecast outcome). John Moore has indicated that he would be prepared to accept £m 700 in 1988-89 (he has not specified his bottom line for later years).

The main points to get across are:

(i) The bids on Health are enormous this year. My offer is already for cash additions which are **twice** the additions made in the two previous Surveys.

(ii) The approach on many of the bids is that of volume planning. This is just not consistent with our cash planning approach. For example, there is a bid to revalue the additions made to meet demographic pressure (£m 63/135/200). It is one thing to recognise the pressures on the Health service from increases in the population and from the growing number of elderly. Appropriate additions were made for this in 1988-89 and 1989-90 in the last Survey. My offer includes £110m for 1990-91. John wants to go further and revalue these additions to compensate for the 0.5% rise in the deflator between the 1986 Survey and the current one.

(iii) Even the huge additions contemplated in my offer make no allowance for Review Body recommendations. John is assuming that any award above the GDP deflator in 1988 will have to come from the Reserve.

(iv) Although his bids have apparently been reduced by significant sums, there has been little real movement on his part. Most of the difference arises from dropping the bid for future Review Body pay, and from our decision not to attempt to calculate AIDS treatment costs beyond 1988-89.

(v) If John is adamant that more money is necessary, he could abolish the welfare milk scheme. This would release £95m for use elsewhere in the Health programme (there is no need to offer full cash compensation, as was done when entitlement was removed from those on family income support, because the social security reforms concentrate help on poor families with children via the Family premium of £6.10 per week). John seems to share my view that the scheme is an anachronism. But he has apparently been swayed by his senior medical advisers, who threaten that damage to children's health would result from abolition of the scheme. Abolition from April 1989 would be acceptable; and if necessary, we could agree that the savings should be split between the Health and Social Security programmes.

It will be particularly difficult if John mentions his wish to see the HCHS programme grow by 2% in real terms in 1988-89. It is vital to get him to think in terms of a cash addition. If you increase our offer to £630 million, and he sticks at £700m for 1988-89, then we could move to £700m, **provided the addition is earmarked for Review Body pay.**

ie we would have provision earmarked for more than just the GDP deflator: Mr Moore would have to use that to meet the first part of the Review Body recommendations, but if the recommendation was still higher he would be able to seek additions from the Reserve.

Jill Rutter

pp **JOHN MAJOR**

(Approved by the CST and signed in his absence).

Annex A

			Mr Moore's bid
i)	B1(b)	Changed inflation assumptions	63/135/200
ii)	Other HCHS bids:-		
	B3	Pressures on acute hospital sector	35/74/116
	B4(a)	Continuation of waiting list initiative	0/28/29
	(b)	Specific targets for waiting times	5/36/41
	B5	RAWP bridging fund	15/32/34
	Breast cancer screening:-		
	B11	- current	9/19/20
	B17	- capital	7/8/0
			71/197/240
(iii)	Use of income generation		20/52/73
(iv)	Centrally Financed Services:-		
	B20	AIDS prevention campaign	19/21/23
	B21	NHS support services	11/11/11
			30/32/34
v)	Abolition of welfare milk		0/0/0*
			184/416/547

* Savings potential 0/-95/-100 to be spent on other health bids.