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HMT MINISTERIAL SPEECHES

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CST 14/5/86

SCOTTISH PARTY  
CONFERENCE



prop



Miss O' MARA

cc PPS  
PS/FST  
PS/MST  
PS/EST  
Sir P Middleston  
Mr KER BUTLER  
Mr CROPPER  
Mr ROSS-GOODBY  
Mr TYRIE

SCOTTISH PARTY CONFERENCE

I attach a final draft of the Chief Secretary's speech to the Scottish Party Conference tomorrow (14 May).

Paul Taylor  
13-5-86



THE RT HON JOHN MacGREGOR OBE MP  
SPEAKING AT THE SCOTTISH CONSERVATIVE AND  
UNIONIST ASSOCIATION ANNUAL CONFERENCE  
IN PERTH

SAID:

It is a great honour for me to speak at this conference today and I am delighted to be the first Scottish Minister from a Ministry other than the Scottish Office.

Indeed it is an interesting reflection that of the fifteen Ministers - from many Departments as well as the Scottish Office - 11 are Scots!

And it is as a Scot, well remembering the appearance, problems and attitudes in the Scotland of my youth, that I want to speak to this Motion today, which I happily accept. And I have

two broad themes in responding to the debate, first that the principles underlying this Budget as indeed of earlier ones and of our economic strategy are based on Scottish virtues and values. And second, that while some will continue to whine and others moan, slowly but surely we are seeing the transformation of the Scottish economy. It is perhaps the regular visitor, conscious of Scotland's past problems, who observes it most.

It is perhaps the passing fate of politicians to find, as we did last week, that the policies which are becoming increasingly successful and relevant to Scotland's economy should be the very ones temporarily rejected by the electorate, just as the Prime Minister's outstanding success in getting practical results at the Tokyo summit gained for her widespread international approval should be contrasted with a somewhat different response later in the week at home.



Before I turn to the Budget itself, I would like to say a word about public expenditure which is one of my main responsibilities.

Our objective is and always has been to achieve a sensible balance between public expenditure and taxation.

In the 60s and 70s the slice of the total economy taken by the State seemed to grow inexorably. It rose from 35 per cent in the 1960s to a peak of over 48 per cent, in 1975-76 it was reined back by the IMF but was pointing upwards again by the time we took office. That much higher level was accompanied by

a weakening economy, high Government borrowing and hence high interest rates, stiff tax burdens on modest incomes, British enterprise being stunted.

Bluntly, we inherited a situation in which the Government was spending beyond what the nation could afford. Unless checked, it would be future generations which would pay the price.

It is surely a Scottish virtue not to overspend and over borrow beyond our limits. It is just as strong a Scottish virtue to seek value for money for every pound you spend.

It is these principles we have been applying to public expenditure. We now have it under control, getting back broadly to the proportions of our national wealth which we saw before the profligate years of Labour spending. And we now have



reduced Government borrowing steadily to prudent levels. This achievement, easy to state, hard to bring about, is undoubtedly contributing to the growing underlying strength of our economy.

But - and this is the crucial point - we have throughout had a clear idea of priorities. While containing expenditure overall, we have quite deliberately increased spending in many areas which we judged to be in the national interest; and which I believe accord with the public's own choices.

Since I became Chief Secretary, I have been struck by some of the curious ironies on the public expenditure front. That you get little credit from those who earlier were vociferous in their complaints about waste in public services when you succeed in cutting it out and getting better value for money; you are accused of cuts or lack of care when in fact you are switching more of every pound spent into real care.

Why a whole new hospital built gets less media coverage (public attention?) than a single old ward closed.

That the services which you are accused of cutting are the ones on which you are spending more than ever before.

Of course what matters is what you spend year on year after taking account of inflation. A 20 per cent increase in cash does not count greatly if inflation has gone up 20 per cent at the same time. But if it goes up 20 per cent ahead of inflation, that is a real increase, in real terms.

And it is in the areas of greatest public concern that our record compares most favourably with the last Labour Government's, in real terms.



Let me take those which I have noticed featuring in the media in the last few days.

On roads, our capital expenditure is up by about a quarter in real terms since 1979.

In the health service we have an unparalleled record with spending up over 20 per cent in real terms since 1979. And it shows in the numbers of staff in front line care, in the new hospitals, in the many more patients being treated. Here in Scotland the number of nurses are up by 11 per cent, of doctors and dentists by almost 9 per cent, and of professionals like radiographers and physiotherapists by as much as 21 per cent. Since 1979 42 major new hospital developments have been completed in Scotland with a £260 million hospital building programme

currently underway for 25 major developments. Patients treated are up by 10 per cent over the latest 5 year period. In cardiac surgery increased funding has taken the number of operations from 790 in 1980 to 1,800 in 1984.

In education, rightly Scotland's pride and I speak as a product, expenditure per pupil in Scottish schools is at an all time high - over 25 per cent in real terms since 1979 and the number of students in higher education in Scotland has increased from 68,000 when we took office to 78,000 in 1984-85.

You know these are the facts. You know we have the right priorities. But because we have also been concerned to ensure good housekeeping, to get good value for money, to be careful



in how we spend because we know there is no magic bottomless pit - it all comes from us as taxpayers - the public has not always got the message. It is up to us to get that message across, to demonstrate how Conservatives are actually caring in practice, by constantly pointing out these improvements locally and on the ground.

But of course caring for public services does not just mean more extra cash resources. Just as in education it is every bit as much about quality and standards and the modern relevance of what is taught, so in the health service cutting out waste and getting more efficient management is just as important.

Much unsung. If fear, we have been putting increasing emphasis on this aspect, for public expenditure control is as much about achieving more in goods and services for a given unit of taxpayers money as it is about simply controlling the amount of money going in. Let me give you just a tiny few of the results.

In central government departments, efficiency scrutinies have brought savings of £300 million a year and multi departmental reviews have led to targets to save £400 million a year on government purchasing within two years, and £50 million in office accommodation.

In defence, competitive tenders have saved £60 million on the estimated cost of the new RAF trainer, and £100 million on the production contract



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In the health service, we are planning for £150 million of efficiency savings now.

We are getting 20 per cent more roads for the same amount of money as we were getting 5 years ago.

Contracting out of services for central government and the national health service has brought a net saving of £50 million a year.

This may sometimes give the impression of an eagerly cost cutting government. In fact the reverse is the truth. Because it is when you get down to what these savings mean in terms of increased goods or services elsewhere that their true worth becomes clear.

The saving in the reduction in the number of civil servants to administer public spending equals the building of 20 new hospitals a year - and we are building them. The savings in defence amount to more than the cost of a type 23 frigate, of 10 new Harriers or of over a 100 new Challenger tanks. These too are public expenditure achievements of which we should be proud.

Of course it is easy to portray increases which are not as much as the interests pressing for them would like as "cuts" in the headlines. And of



course for some people you cannot ever spend enough, irrespective of the consequences for the taxpayer or the economy as a whole.

That's Labour's way. Labour front bench spokesmen have been making promises all over the shop. But we have rumbled them. We have added up the costs and you will have seen that I have now costed it at £24 billion. That is what they would spend on top of existing spending programmes, once they were in full swing. It amounts to an increase of 26 per cent on VAT. That's a message for the doorstep.

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Our greatest danger is short memories. It is up to all of us to jog them. For what did these policies bring last time? Bursts of enthusiastic and heady spending. Priorities for spending planned by the unions. Those were the days of social contracts. Contracts to print money and debase the currency. Labour leaders stood at the bar and bought their supporters round after round of drinks. And it went on the slate.

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Of course I recognise that there are still problems in the Scottish economy. Of course there are areas where jobs are still dependent on the old heavy industries which they <sup>are</sup> ~~weld~~ over capacity or an acute shortage of demand. Of course there are challenges and much still to be done - there always will be.

But Scotland is one of the best examples in Western Europe of the gradual transformation from the old to the new. It takes time to convince those with girders in their bones that a good man's job in manufacturing industry doesn't just mean bashing heavy metal. Silicon Glen so often on people's lips, the success of companies like Ferranti and British Aerospace, the high standards and good service now in the tourist industry, capitalising properly on one

+2,000 (net)  
in 1984

of Scotland's assets and not the mournful business it was in my youth when to provide service thought to be servile, the growth of new and small businesses (give figures) and the success of projects such as BSC (Industries) at Glen Garnock, all these point the way ahead in a highly competitive world.

It has been accompanied by the change in the environment, both physical and cultural, of which the increasing transformation of Glasgow into a city again of many attractions is a symbol.

Where once there was a lack of enterprising businessmen and go-ahead managers, so that the complaint was that everything always happened down south, now the home grown businessmen are thrusting forward, mingling with the entrepreneurs from overseas who were attracted by this environment.



Where once there was a lack of confidence, the confidence is returning. Where once there was a begging bowl mentality - the only good thing to come out of England, and always demanded, was bigger taxpayers handouts and companies, so it seemed, could only survive in a sea of subsidy; today there is still high public expenditure yes, in infrastructure and in public services, but companies are thrusting forward through enterprise, working for markets and throwing off old bad habits. The new approach of the SDA under a Conservative government, with its emphasis on commercial enterprises and free market attitudes, its blend of modest public expenditure and much larger private investment, its use of public funds not as a chuck but as a catalyst, and fiscal changes we have introduced to encourage enterprise and risk taking have helped to bring about this change of mood.

Of course it takes time for these changes to work down through the system, to change long held public attitudes and people's perceptions of themselves. All our Scottish opponents have a gloomy view of Scotland and it is that picture they keep portraying elsewhere. It is in their interest to keep Scotland down. A self-confident people does not seek socialism or inward looking nationalism. What we are about is boosting the confidence of Scotland, improving the quality of life and we simply must not allow ourselves to be talked down.

And the results are showing through.

If Britain was once near the bottom of the European growth league, Scotland was in relegation zone.



But today while the growth in the British economy is among the highest of industrialised nations, Scottish output has been ahead of the UK average. Where in the last 6 years manufacturing productivity in Britain has averaged 3½ per cent a year compared with 1 per cent in the previous 5 years, Scotland has done even better.

Where Scotland's income per head or level of employment were once among the worst in the country, today Scotland is third only to the South East of England and East Anglia.

Scotland's economy is being revitalised. Scotland, now one of the more prosperous regions of the UK, has

led the way and is meeting the challenge of world markets. Scotland has shown how an ageing and traditional economy can be superseded and transformed into one better equipped to flourish in the last decade of the 20th century.



This motion rightly emphasises certain features of the Budget which are crucial to our economic strategy and to our vision of society. I would like to pick out just a few features.

First, the encouragement of the capital <sup>own</sup> earning democracy. While Edinburgh as a key financial centre had long epitomised the values of savings and thrift, and it was the instinctive aim <sup>of</sup> many Scots to ensure through hard work and canny investment financial independence for their families, in some respects Scotland lagged behind. There was another powerful streak, an over dependence in housing on the town council landlord.

But the success of the council house sales policy, spreading the thrill of home ownership to many who could

78,000  
already  
exercised  
rights  
to  
buy.

have never previously have contemplated before, taking root in Scotland too (possibly quote figures). And now we are making big strides forward in the next stage of direct ownership, to shares. Successive Budget policies, encouragement to the small investor to take up for the first time shares in companies such as BT, and now in this latest Budget the Personal Equity Plan, will all help to bring this about. Already we are achieving greater success than many of us had dared hope. A recent market research survey has suggested that here in Scotland something like 13 per cent of the ~~(adult?)~~ population, or some <sup>over 1/2 m</sup> ~~(?)~~ people, now own shares direct. The old Scottish instincts are reviving.



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CST 5/7/86

CONSERVATIVE POLITICAL  
CENTRE



APR-2  
PUP

FROM: G W MONGER  
DATE: 3 July 1986

MR PEGLER,  
APS/CHIEF SECRETARY

cc PS/Chancellor  
PS/Financial Secretary  
Miss O'Mara  
Miss Sinclair  
Mr Tyrie

C/ see note below

CR 3/7

PS/IR

**CHIEF SECRETARY'S SPEECH, 5 JULY**

A couple of points on the taxation section of the speech.

2. Would not "tax reduction and reform" be a better heading? (page 10).
3. On the last line on page 10 you could insert after 35% the words "(29% for small companies)".
4. On the second paragraph on page 11, it is rather an exaggeration to say "we have indexed CGT". Indexation does not apply to pre-1982 gains, and this is one of the main complaints about the tax. You could say: "We have ensured that in future CGT will apply only to real gains and not paper gains".
5. In the next paragraph, it seems surprising that there is no reference to the aim of reducing the basic rate to 25%, especially since the aim of increasing allowances is mentioned.
6. In the last section, should there not be a reference to further tax reductions as one of the Government's long term aims? It is perhaps implicit in "giving people the freedom to spend more of their own money", but it seems important enough to be worth stating explicitly.

G W

G W MONGER



Mr TYRIE

cc

PPS

ppp

PS/ST

PS/MSI

PS/EST

SIR P. MIDDLETON

SIR T. BURNS

MR FER BUTLER

MR MONCK

MR MONGER

MR TURNBULL

MR CULPIN

MR GRIMSTONE

MISS O'MARA

MR PICKERING

PS / IR <sup>MR STREMER</sup>

CHIEF SECRETARY'S SPEECH : 5 JULY: CONSERVATIVE POLITICAL CENTRE  
to attach a copy of the final version of  
the Chief Secretary's speech for Salvadorans.

Paul Legler  
4-7-86



**THEMES IN ECONOMIC POLICY**

In 1979 the Government set about changing the balance between the individual and the State. It encouraged enterprise, and property and share ownership. It decisively rejected the encroaching and throttling power of the State in favour of more personal responsibility and freedom. Our policies mark a decisive break from the belief that only Government action is effective and display a determination to get to grips with the growth in the size and power of the State.

Few doubt that these are the hallmarks of the Conservative approach. We have been succeeding in shifting the balance of argument, philosophy and ideas in British politics decisively our way. The consolidation of that success will be the challenge for Conservatives in the next election and beyond.

Now there are many ways in which this Government has broken new ground, where we have succeeded where others have not, or have not even tried. The sharp reduction in inflation to levels more comparable to those of our major competitors overseas; the thrust for greater efficiency and competitiveness; enabling managers to manage, to root out restrictive practices and overmanning in our industry and commerce; the refusal to prop-up outdated industries: the restoration of democracy to our trade unions; above all good housekeeping and sound finance. All these are aspects of this Government where the pace and degree of achievement has been considerable, and where Mrs Thatcher's drive and leadership has been so critical.

But there are other key themes of Conservatism, again so often articulated and personified by Mrs Thatcher, which are certainly not in my view bolts from the blue. Today I want to concentrate on these, which I believe show that there has also been much consistency in Conservative thinking; that there is a clear thread of distinctly Conservative ideas which connect today's policies with the Conservatism of 15, 20 or 25 years ago. -



At this conference you are discussing ideas for the future which will sustain the Tory party into a third term and beyond. The four central areas I wish to pick out today all demonstrate that consistency of Conservative philosophy and practical ideas which I hope will provide clues to the direction of Conservatism in the future. And I deliberately choose such themes, because we are sometimes accused of pursuing policies piece-meal, without a consistency of purpose or philosophy behind them. That is the impression some may get because of the Parliamentary process. Media attention is focussed on the detailed policy issues of the day. It is on occasions like this that we can group the policies together and demonstrate the consistent threads that have been running through them.

The four I have chosen are:-

- (i) Personal ownership and responsibility, the development of the property owning democracy into popular capitalism.
- (ii) Privatisation.
- (iii) Tax Policy.
- (iv) The control of public expenditure.

I do not pretend that all the Government's policies have direct antecedents. Nor does the Conservative party have some overarching blueprint which it is implementing with mechanical determination. That is certainly not the Conservative way. I only wish to suggest that there is a consistency in our intentions and our thought that has not had the attention it deserves; a consistency that is a guide to our future actions.

## **1. Personal ownership and responsibility**

In 'The case for Conservatism' published nearly 40 years ago, Quintin Hogg as he then was said "We may be a long way off it, but this is the ideal - a "property owning democracy".



No government has made a greater contribution to making a reality of his ideal; and no single measure typifies this Government's approach better than the Housing Act of 1980; which as you know gave council tenants the right to buy their properties at a discount.

The boldness of the step is, perhaps with privatisation, the clearest proof of the Government's radical credentials. At a stroke the Government changed the terms of the debate. Other Parties were forced to readjust. Labour initially clung to a commitment to withdraw the right to buy. It was a gesture of desperation from a party which saw their council estate strongholds broken up by the exercise of new freedoms by the tenants themselves.

When the pamphlet was written, owner-occupation was below 30%. Under this Government it has risen from 55% to 62%. Nearly one million public sector dwellings have been sold.

This Government's support for property is based on the same beliefs as its Conservative predecessors, that the possession of property by the individual adds greatly to his personal fulfilment, his security and his opportunity to build up an asset for himself on his retirement and for passing on to his family in due course. And with these come a much greater appreciation of and willingness to undertake personal responsibility. Pride of ownership does far more than the State ever could, to maintain the fabric of cities, towns and villages.

Once again, council house sales should not be seen as a bold departure from Conservative thinking. Far from it. It was a Conservative Government which, in the Housing Act of 1957, gave local authorities the power to sell council homes. By 1968 council house sales had reached 13,000 a year and predictably, it was a Labour Government which took the decision to limit council house sales to a bizarre formula - a quarter of one percent of the total council housing stock in the four



conurbations - Greater London, West Midlands, South-East Lancashire and Merseyside.

For most, the prospects of ownership of capital starts with the home. But this Government has built on that foundation and taken far bolder steps than its Conservative predecessors.

We have greatly encouraged wider share ownership, giving individuals direct participation in the creation of wealth.

The list of measures is an impressive one.

In the the last Budget we announced the personal equity plan, an innovative scheme to encourage the growth of individual share ownership. In six of the last seven Budgets, we have taken measures to encourage employee share ownership. Those measures are bearing fruit~~s~~. In 1979 there were only 30 all employee schemes. Now there are over a thousand. They cover 1½ million employees owning or holding options on shares with an original value of fl½ billion. Moreover there is a link between the huge extension of home ownership and wider share ownership. For soon millions of families will, as a first generation of new house-owners passes on, find that for the first time in their lives and indeed their families' history they have quite significant "free" assets of their own to invest.

Just as people are enjoying more of the benefits of property and capital ownership so they are also more prepared than before to take on the responsibility of starting up new businesses and in becoming self-employed. Since March 1979 there has been a massive increase in the self-employed of 761,000. Similarly 130,000 of net new businesses were created between 1980 and 1984. More people than ever before are also starting personal pension plans, taking on the responsibility of looking after their own retirement.

We have set up the Business Expansion Scheme which during its first 2 years enabled over £252 million to be raised by over



20,000 investors. This scheme has helped fill an important financing gap for small companies while at the same time further encouraging the growth of wider share ownership.

We have helped stimulate the growth of venture capital and have encouraged the development of active markets outside the stock exchange in unlisted securities. The OTC market provides an early opportunity for capitalising high risk projects. The USM is the natural home of young companies looking for dynamic growth.

And perhaps nothing is so illustrative of the dramatic shift in attitudes towards entrepreneurship, risk and reward than the 40 fold increase in venture capital invested between 1979 and 1985.

In privatised companies we have encouraged wage earners to become capital owners. Over 80% of employees in privatised companies have become shareholders.

## 2. Privatisation

The merits of wider home and share ownership by individuals are much better understood than they were only a few years ago. Likewise we have decisively changed attitudes on what it is sensible for the State to own.

When we came to office in 1979, we inherited a sizeable state industrial sector that accounted for over 1/10th of the UK's gross domestic product and 1/7th of the nation's annual total investment.

Privatisation has not been pursued merely because Conservatives believe in private property, good enough reason though this would be. Privatisation has been pursued also because the disciplines of the market place usually help best to create the wealth on which we all depend. Commercial enterprise flourishes better in private hands than under State ownership.



We all have our own stories to tell of the inefficiencies of some nationalised industries with which we have had daily contact. The discipline of the market is the most effective way of tackling these, better than any number of Select Committee Reports or Whitehall investigations. Similarly, it is the discipline of the market which concentrates the mind of management best on how to use economic resources, on how to allocate investment most effectively.

Privatization has brought results. Take the National Freight Corporation: between 1975 and 1979, NFC ran up cumulative losses of over £70m. Now this is a major success for road haulage business, diversifying into other areas. Profits have increased seven fold since privatisation and the value of employees shares in the consortium have gone up by no less than twenty-seven fold.

Take Jaguar: pre-tax profits are up 33% in 1985 compared with 1984. Production is at record levels and 1,100 new jobs have been created.

Take British Aerospace: pre-tax profits have almost trebled since privatisation in 1981, and the order book at the end of 1985 is at a record £5 billion.

This is the kind of performance which privatisation can stimulate. So far, 12 major companies have been sold to the private sector representing 1/5th of the State sector.

## Conclusions Sections 1 and 2

### **The case for property**

On the case for property, as on so many issues, this Government has decisively changed attitudes. Not long ago nationalisation was seen as an irreversible transfer of power and control to the State. Similarly, not long ago it was conventional wisdom



to see the dwindling number of small shareholders at the expense of the big institutions as inevitable. This Government has shown that the tide of nationalisation can be reversed. By the end of 1987, almost half of the State commercial sector will have been put back into private hands. While halving the State commercial sector we have doubled the number of small shareholders. Taken together this represents an almost revolutionary decentralization and diffusion of power to individuals at the expense of the State.

### 3. Tax reduction and reform

Conservatives do not see any particular merit in high taxation. Taxation is of course necessary to raise the revenue to pay for defence, law and order, education, health and social services, and other public services. But if tax is too high it stifles enterprise, blunts incentives and makes the economy less efficient. On the whole Conservatives do not believe that civil servants and Governments are better judges on how to spend money than individuals. It follows that no Government should take more than it really needs.

Conservatives have been guided by the twin objectives of first getting tax down and, secondly reforming and simplifying it. It is no accident that the US and Japan have the lowest level of tax as a proportion of national income and are also the most successful economic performers in recent years. A less burdensome and simplified tax system will improve economic performance and foster a climate favourable to the creation of wealth and jobs. Only by creating that wealth can we pay for improved social services.

We have already taken many steps to reduce the burden of personal taxation by reducing the basic rate from 33 to 29 pence in the pound, by bringing the top rates of tax down, by increasing personal allowances substantially in real terms. Corporation tax at 35% - 29% for small companies - is now the lowest of any major industrialised country. Stamp Duty has been reduced first to 1% and now to  $\frac{1}{2}$ % on shares.



Similarly we have reformed and simplified the system. So far we have abolished four taxes, the National Insurance surcharge, Development Land Tax, Investment Income surcharge and Capital Transfer Tax on Lifetime Giving. We have switched taxes on earnings to taxes on spending. We have ensured that in future CGT will apply only to real gains and not paper gains. We have also provided incentives for enterprise and popular capitalism through the Business Expansion Scheme and the Personal Equity Plan Scheme announced in the last Budget.

There is still much more to be done. In particular, the burden of tax on average and below average incomes is still too high and the <sup>tax</sup> treatment of marriage and in particular of the married woman badly needs reform - hence our Green Paper on "The Reform of Personal Taxation".

Perhaps our tax policy can be best summarised by a manifesto quotation.

"We will reduce taxation. We will simplify the tax system. We will concentrate on making progressive and substantial reductions in Income Tax....High taxation discourages effort and saving, deadens the spirit of enterprise and causes many of our best brains to leave the Country."

That was not in the manifesto of 1983, nor 1979, but 1970.

Socialists of course like high taxation. In the early 1970s Mr Healey excited Labour Conferences with the prospect that the rich would be squeezed until the pips squeaked. With Labour's marginal rates of tax on earned and investment income at 83% and 98% respectively it would be no exaggeration to say that tax had become legalised robbery. Recently we have been treated to similar outbursts from Mr Hattersley who singles out those he describes as the "bloody rich" for his special brand of tax treatment.



Posing awkwardly as Robin Hood he suggests that the restoration of Labour's penal tax regime on the top 5% of income earners at 1979 rates will enable £3.5 billion more of social service spending. But as so often with Mr Hattersley he has not done his sums. To raise the money he would need, as well as returning to the punitive CGT, CTT, IIS regimes of the last Labour Government, to impose a 70% marginal rate of Income Tax on those with taxable income over £18,600. A married couple, both teachers, for example, would be paying tax at this ludicrous rate. So Mr Hattersley's green tights are splitting and underneath his ill-fitting suit of Lincoln green we find the Sheriff of Nottingham after all.

#### 4. Public Expenditure

A central aim of Government economic policy has been to reduce the burden of public expenditure as a proportion of the total economy. The ratchet is the right metaphor to describe the growth of public expenditure in the post-war years. As each notch was reached public spending created its own constituency and its own pressure group to support it. Getting public expenditure under control has been a truly rasping experience, but one we were determined to undertake.

The achievement cannot be underestimated. We have kept public expenditure to levels we can afford.

By controlling public expenditure and borrowing, by sound finance in general, we have been able to get inflation and interest rates down. The experience of the late 1970s gives us the clearest example of how the loss of control of public expenditure leads to the loss of control of the whole of a nation's public finances, soaring foreign debt and spiralling inflation.

On public expenditure we have also kept two other objectives firmly in mind:



- The allocation of spending to priorities within the overall total
- Value for money.

Within the public expenditure totals that can be afforded we have undertaken a regular, rigorous and sensitive appraisal of priorities. In the late 1970s Labour ran down our defences. In 1979 defence clearly had to be a priority, and despite the recession we found the money: we have increased defence expenditure, excluding Falklands expenditure, by 16% in real terms since 1979.

A careful appraisal of our priorities will enable us to spend more on other key services. This we are already achieving. On health, spending is up 24% in real terms; expenditure on benefits for the long-term sick and disabled is up by 50% in real terms.

We can also make money available to priority areas by keeping costs down, by getting value for money. We have generated efficiency savings amounting to more than £1 billion since 1979 in the NHS.

Those savings came from better management, and careful planning, competitive tendering and cutting out waste. They are the equivalent to 25 new hospitals. In defence competitive tendering has saved £60 million on the estimated cost of the new RAF trainer, and £100 million on the contract for the Army's new infantry combat vehicles. This is enough to pay for a new frigate or a squadron of vertical takeoff Harriers.

We have also made the administration of Central Government more efficient. We have reduced the size of the civil service by nearly 20%, representing a net saving of more than £¼ billion on the civil service pay bill.

And how have the savings been achieved? By improvements in efficiency, greater use of new technology, cutting out



unnecessary work and by privatisation and contracting out. Nor have these savings been made at the cost of a good service. The productivity gains we have made often go hand in hand with improvements in the level of service. For example, in the Job Centres the cost of placing each person in a job has been significantly reduced at the same time that workloads have increased and the range of services to employers and job seekers has been broadened.

I am confident that these are the right policies. They have enabled us to put the boom and bust of the Labour years firmly behind us.

It was during the 1974-1979 Labour Government that the division between the parties sharpened acutely, as Labour swung so much to the left. The 1979 election gave us our opportunity to bring out the contrast, and with a determined leader who has never lost sight of our principal goals to shift radically the climate of opinion, and to make possible what many of us had come into politics to achieve. It was our opportunity to work for those things that would give the individual more liberty and responsibility:

- in homes and savings
- in the rejection of nationalisation
- in the need to reform the unions
- in lower taxation
- in the control of public expenditure

The Conservative Party had been developing this message in the 1960s for it is a message which springs from our values. But when tested in 1974 the electorate was not ready to go for the big break. The greatest achievement of the past seven



years has been a decisive rejection of the resigned acceptance to nationalisation, to the growth in union power, to the diminution in the control in people's lives, to an ever larger proportion of taxation and public expenditure taken up by the the State.

Completing the changes we have put in place is our task for the next ten years.

First we must ensure that the spread of property ownership will become an explosion of capital and share ownership by much of the population. 'Everyone a capitalist' will be our goal.

Second, we shall develop policies to give people the freedom to spend more of their own money , not only for themselves but to enable them to exercise their own natural generosity. The reforms which we put through on Charitable Giving in the last Budget are a model of the kind of reforms which are integral to the kind of society Conservatives want to see.

Third, we shall develop policies which encourage a sense of individual responsibility towards these very things for which Labour thinks only the State should be responsible. For example, should almost all the funds for State schools always come exclusively from the State?

Property, freedom, responsibility, these mean a lot to Conservatives. But Conservatives are not motivated by a burning ideology. These policies will be implemented in a British way, with due respect to the traditions which have made Britain such a stable and pleasant place in which to live. They will be implemented gradually, with a proper scepticism for blueprints and plans.

The aim of Conservative reform has been to contain the power of the State and to create a framework in which individual responsibility can flourish and prosper, economically as well



as spiritually. But new policies alone do not suffice. In 1979 the country badly needed a change in style and leadership, more honest and responsible, less dominated by political expediency.

The contribution of the Conservatives over the past seven years has been to provide fresh ideas and bold leadership. As De Tocqueville said:

"without ideas and leaders, a people cannot truly be said to exist."





PUT



C/

Below are three CST  
speeches - 2 still  
drafts + 1 final  
version

CR 3/7

CST has decided not

to press release anything  
from his CPC speech.

He wants to work on it  
further before delivery.

It will be published idc.



Mr TYRIE

cc PPS

still some figs etc missing from this speech, but CST'S office thought this was a good point for you to look at it.

CR 3/7

PS/TSR

PS/MSI

PS/EST

SIR P MIDDLETON

SIR T BURNS

MR FER BUTLER

MR MONCK

MR MONGER

MR TURNBULL

MR CULPIN

MR GRIMSTONE

MISS O'MARA

MR PICKERING

PS/IR

CHIEF SECRETARY'S SPEECH : 5 JULY: CONSERVATIVE POLITICAL CENTRE

I attach a draft of the Chief Secretary's speech for Saturday. I would be grateful if you and copy recipients would check for accuracy and insert figures etc. as necessary. Comments should reach me by 3 pm tomorrow (Thursday 3 July).



2 At present the Chief Secretary has had an opportunity to look at the draft only as far as page 12. He will be revising the rest of the draft overnight and I will circulate the amended version as soon as possible tomorrow morning. Meanwhile I would welcome any comments on the existing draft from page 13 onwards in the same timescale as above.

Paul Legler

2 July 1986



**THEMES IN ECONOMIC POLICY**

In 1979 the Government set about changing the balance between the individual and the State. It encouraged enterprise, and property and share ownership. It decisively rejected the encroaching and throttling power of the State in favour of more personal responsibility and freedom. Our policies mark a decisive break from the belief that only Government action is effective and display a determination to get to grips with the growth in the size and power of the State.

Few doubt that this is the hallmark of the Conservative ~~appraisal~~ <sup>approach</sup>. Many would say that we are succeeding in shifting the whole balance of British politics in our direction, so that the middle-ground of argument has moved decisively our way. The consolidation of that success will be the challenge for Conservatives in the next election and beyond.

Now there are many ways in which we have broken new ground, at least in terms of contemporary <sup>or</sup> politics, where we have succeeded where others have not, or have not even tried. The sharp reduction in inflation to levels more comparable to those of our major competitors overseas; the thrust for ~~private~~ <sup>greater</sup> efficiency and competitiveness, the enabling managers to manage, to root out restrictive practices and overmanning in our industry and

*smaller  
ways  
that are  
different!*



commerce; the refusal to prop-up outdated industries: the restoration of democracy to our trade unions; above all good housekeeping and sound finance. All these are hallmarks of this Government where the pace and degree of achievement has been considerable, and where Mrs Thatcher's drive and leadership has been so critical.

But there are other key themes of Conservatism again so often articulated and personified by Mrs Thatcher, which are certainly not in my view bolts from the blue. Today I want to concentrate on these, which I believe show that there has also been much consistency in Conservative thinking that there is a clear thread of distinctly Conservative ideas which connect today's policies with the Conservatism of 15 ,20 or 25 years ago.

At this conference you are discussing ideas for the future which will sustain the Tory party into a third term and beyond. The four central areas I wish to pick out today all demonstrate that consistency of Conservative philosophy and practical ideas which I hope will provide clues to the direction of Conservatism in the future. And I deliberately choose themes as it were because we are sometimes accused of pursuing policies piece-meal, without a consistency of purpose or philosophy behind them. That is the impression some <sup>a</sup>my get because of the Parliamentary process. Media attention is focussed on the detailed policy issue of the day. It is on occasions like this that we can group the policies together and demonstrate the consistent threads that have been running through them.



The four I have chosen are:-

- (i) Personal ownership and responsibility; the development of the property owning democracy into popular capitalism.
- (ii) Privatisation.
- (iii) Tax Policy.
- (iv) The control of public expenditure.

I do not pretend that all the Government's policies have direct antecedents. Nor does the Conservative party have some overarching blueprint which it is implementing with mechanical determination. That is certainly not the Conservative way. I only wish to suggest that there is a consistency in our intentions and our thought that has not had the attention it deserves; a consistency that is a guide to our future actions.

#### 1. Personal ownership and responsibility

In 'The case for Conservatism' published nearly 40 years ago, Quintin Hogg said "We may be a long way off it, but this is the ideal - a "property owning democracy"". No government has made a greater contribution to making a reality of his ideal; and no single measure typifies this Government's approach better than the Housing Act of 1980, which as you know gave council tenants the right to buy their properties at a discount.



The boldness of the step is, perhaps with privatisation, the clearest proof of the Government's radical credentials. At a stroke the Government changed the terms of the debate. Other Parties were forced to readjust. Labour initially clung to a commitment to withdraw the right to buy. It was a gesture of desperation from a party which saw their council estate strongholds broken up by the exercise of new freedoms by the tenants themselves.

40 years ago owner occupation was [ ]%. Owner-occupation under this Government has risen from 55% to 62%. Nearly one million public sector dwellings have been sold.

This Government's support for property is based on the same beliefs as its Conservative predecessors, that the possession of property by the individual adds greatly to his personal fulfilment, his security and his opportunity to build up an asset for himself on his retirement and for passing on to his family in due course. And with these come a much greater appreciation of opportunity and willingness to undertake personal responsibility. Pride of ownership does far more than the State ever could, to maintain the fabric of cities, towns and villages.

Once again, council house sales should not be seen as a bold departure from Conservative thinking. Far from it. It was a Conservative Government which, in the Housing Act of 1957, gave local authorities the power to sell council homes. By 1968 council house sales had reached 13,000 a year and predictably, it was a Labour Government which took the decision to limit council house sales to a bizarre formula - a quarter



of one percent of the total council housing stock in the four conurbations - Greater London, West Midlands, South-East Lancashire and Merseyside.

For most, the prospects of ownership of capital starts with the home. But this Government has built on that foundation and taken far bolder steps than its Conservative predecessors.

We have greatly encouraged wider share ownership, giving individuals direct participation in the creation of wealth.

The list of measures is an impressive one.

In the the last Budget we announced the personal equity plan, an innovative scheme to encourage the growth of individual share ownership. In six of the last seven Budgets, we have taken measures to encourage employee share ownership. Those measures are bearing fruits. In 1979 there were only 30 all employee schemes. Now there are over a thousand. They cover 1½ million employees owning or holding options on shares with an original value of £1½ billion. Moreover there is a link between the huge extension of home ownership and wider share ownership. For soon million of families will, as a first generation of new house-owners passes on, find that for the first time in their lives and indeed their families' history have quite significant "free" assets *of their own to invest.*

[There needs to be a link para here. All these succeeding paras are a bit difficult for wider share ownership, though they follow on. Para needs to be about encouragement of personal responsibility in creating jobs - self-employed, small businesses and entrepreneurs, etc.]



Personal pensions

need to go

in here

coo.]

We have set up the Business Expansion Scheme which during its first year enabled £105 million to be raised by almost 20,000 investors. This scheme has helped fill an important gap - generating direct equity investment by individuals into small unquoted companies.

We have taken many measures to stimulate the growth of venture capital. The OTC market provides an early opportunity for capitalising high risk projects. The USM is the natural home of young companies looking for dynamic growth.

And perhaps nothing is so illustrative of the dramatic shift in attitudes towards entrepreneurship, risk and reward than the 40 fold increase in venture capital invested between 1979 and 1985.

In privatised companies wage earners have become capital owners. Over 80% of employees in privatised companies have become shareholders.



## 2. Privatisation

The merits of wider home and share ownership by individuals are much better understood than they were only a few years ago. Likewise we have decisively changed attitudes on what it is sensible for the State to own.

When we came to office in 1979, we inherited a sizeable state industrial sector that accounted for over 1/10th of the UK's gross domestic product and 1/7th of the nation's annual total investment.

Privatisation has not been pursued merely because Conservatives believe in private property, good enough reason though this would be. Privatisation has been pursued also because the disciplines of the market place usually help best to create the wealth on which we all depend.

Commercial enterprise flourishes<sup>e</sup> better in private hands than under State ownership. We all have our own stories to tell of the inefficiencies of some nationalised industries with which we have had daily contact. The discipline of the market is the most effective way of tackling these, better than any number of Select Committee Reports or Whitehall investigations. Similarly, it is the discipline of the market which concentrates the mind of management best on how to use economic resources, on how to allocate investment most effectively.

These policies are reaping rich rewards. Take the National Freight Corporation: in the 1970s it had a history of staggering



from one crisis to another, often at the taxpayers expense. (figures). Now this is a major success for road haulage business, diversifying into other areas. Profits have increased seven fold since privatisation and the value of employees shares in the consortium have gone up by no less than twenty fold.

Take **Jaguar**: pre-tax profits are up 33% in 1985 compared with 1984. Production is at record levels and 1,100 new jobs have been created.

Take **British Aerospace**: pre-tax profits have almost trebled since privatisation in 1981 the order book at the end of 1985 is at a record £5 billion.

This is the kind of performance which privatisation can stimulate. So far, 12 major companies have been sold to the private sector representing 1/5th of the State sector.

## Conclusions Sections 1 and 2

### **The case for property**

On the case for property, as on so many issues, this **Government** has decisively changed attitudes. Not long ago nationalisation was seen as an irreversible transfer of power and control to the State. Similarly, not long ago it was conventional wisdom to see the dwindling number of small shareholders at the expense of the big institutions as inevitable. This Government has



shown that the tide of nationalisation can be reversed. By the end of 1987, almost half of the State commercial sector will have been put back into private hands. Likewise, the number of small shareholders has probably doubled.



[Too extreme and  
simplified. Can

### 3. Tax Reform

this be

redrafted]

For Conservatives, tax has always been considered a necessary evil, necessary because we need to pay for defence, law and order, education, health and other social services, but evil because high taxation stifles enterprise, blunts incentives and makes the economy less efficient. Conservatives believe people should be allowed to spend their own money as they like. Individuals are better judges than Whitehall on how to spend money. Spending of individuals makes the economy responsive to changing tastes and circumstances. No government should take more than it really needs.

Conservatives have been guided by the twin objectives of first getting tax down and, secondly reforming and simplifying it. It is no accident that the US and Japan have the lowest level of tax as a proportion of national income and are also the most successful economic performers in recent years. A less burdensome and simplified tax system will improve economic performance and foster a climate favourable to the creation of wealth and jobs. Only by creating that wealth can we pay for improved social services.

We have already taken many steps to reduce the burden of personal taxation by reducing the basic rate from 33 to 29 pence in the pound, by bringing the top rates of tax down, by increasing personal allowances substantially in real terms. Corporation tax at 35% is now the lowest of any major industrialised country.



Stamp Duty has been reduced first to 1% and now to ½% on shares.

Similarly we have reformed and simplified the system. So far we have abolished four taxes, the National Insurance surcharge, Development Land Tax, Investment Incomes surcharge and Capital Transfer Tax on Lifetime Giving. We have switched taxes on earnings to taxes on spending. We have indexed CGT. We have also provided incentives for enterprise and popular capitalism through the Business Expansion Scheme and the Personal Equity Plan Scheme announced in the last Budget.

There is still much more to be done. In particular, too many people come into tax at too low a level of income and the treatment of married men and women for income tax is still unequal.

Perhaps our tax policy can be best summarised by a manifesto quotation.

"We will reduce taxation. We will simplify the tax system. We will concentrate on making progressive and substantial reductions in Income Tax....High taxation discourages effort and saving, deadens the spirit of enterprise and causes many of our best brains to leave the Country."

That was not in the manifesto of 1983, nor 1979, but 1970.

It might seem commonsense that tax should be regarded as a necessary evil but it must be remembered that for the Labour



Party it is a tool for changing society.

Socialists like high taxation. In the early 1970s Mr Healey excited Labour Conferences with the prospect that the rich would be squeezed until they howled. With Labour's marginal rates of tax on earned and investment income at 83% and 98% respectively it would be no exaggeration to say that tax had become legalised robbery. Recently we have been treated to similar outbursts from Mr Hattersley who singles out the "bloody rich" for his special brand of tax treatment.

Posing awkwardly as Robin Hood he suggests that the restoration of Labour's penal tax regime on the top 5% of income earners at 1979 rates will enable £3.5 billion more of social service spending. But as so often with Mr Hattersley he has not done his sums. To raise the money he would need to impose a 70% marginal rate of Income Tax on tax units earning over £17,600. A married couple, both teachers, for example, would be paying tax at this ludicrous rate. So Mr Hattersley's green tights are splitting and underneath his ill-fitting suit of Lincoln green we find the Sheriff of Nottingham after all.



#### 4. Public Expenditure

A central aim of Government economic policy has been to reduce the burden of public expenditure as a proportion of the total economy. The ratchet is the right metaphor to describe the growth of public expenditure in the post-war years. As each notch was reached public spending created its own constituency and its own pressure group to support it. Getting public expenditure under control has been a truly rasping experience, but one we were determined to undertake.

The achievement cannot be underestimated. We have kept public



expenditure to levels we can afford and in doing so we have maintained the levels of spending needed on vital social policies, on the NHS and education for example secure for the future.

By controlling public expenditure and borrowing we have been able to get inflation and interest rates down. The experience of the late 70s gives us the clearest example of how the loss of control of public expenditure leads to the loss of control of the whole of a nation's public finances, soaring foreign debt and spiralling inflation.

On public expenditure we have also kept two other objectives firmly in mind:

- The allocation of spending to priorities within the overall total
- Value for money.

Within the public expenditure totals that can be afforded we have undertaken a regular, rigorous and sensitive appraisal of priorities. In the late 1970s Labour ran down our defences. Defence clearly had to be a priority, and despite the recession we found the money: we have increased defence expenditure by x% in real terms since 1979.

A careful appraisal of our priorities will enable us to spend



more on other key services. This we are already achieving. On health, spending is up 24% in real terms; expenditure on benefits for the long-term sick and disabled is up by 50% in real terms; spending per pupil in education is now at record levels.

We can also make money available to priority areas by keeping costs down, by getting value for money. We have generated efficiency savings amounting to more than £1 billion since 1979 in the NHS.

Those savings came from better management, and careful planning, competitive tendering and cutting out waste. They are the equivalent to 25 new hospitals. In defence competitive tendering has saved £60 million a year on the estimated cost of the new RAF trainer, and £100 million on the contract for the Army's new infantry combat vehicles. This is enough to pay for a new frigate or a squadron of vertical takeoff Harriers.

We have also made the administration of Central Government more efficient. We have reduced the size of the civil service by nearly 20%, representing a net saving of more than £¼ billion on the civil service pay bill.

And how have the savings been achieved? By improvements in efficiency, greater use of new technology, cutting out unnecessary work and by privatisation of contracting out. Nor have these savings been made at the cost of a good service. (The productivity gains we have made often go hand in hand with improvements in the level of service. For example, in the Job Centres the cost of placing each person in a job has been significantly reduced at the same time that workloads



have increased and the range of services to employers and job seekers has been broadened.)

I am confident that these are the right policies. They have enabled us to put the boom and bust of the Labour years firmly behind us.

But Conservative supporters would recognise these policies from earlier Tory governments. Between 1970 and 1973 it was a Conservative Government which held the share of public expenditure as a proportion of the national income steady in real terms. Nor was the emphasis on value for money so new. The 1970 manifesto read:

"There will be cost reduction plans for every single ministry in Whitehall, and the widespread application throughout Government of the most modern management, budgeting and cost-effectiveness techniques."

It really should be no surprise that successive Conservative Governments have sought to be prudent with taxpayers' money, to use commonsense to allocate it to priorities and to find ways of making the same money buy more. These are things that Conservatives will always seek to do.

The very office of State which I hold was created by a Conservative Government. The job of Chief Secretary was created in 1961 because that Conservative Government felt it essential to have a minister solely responsible for Government expenditure.



## Conclusion

At one time it seemed that the benefits which spring from a property owning democracy - a balance between the state and the citizen which gives the individual liberty and responsibility - could be taken for granted in Britain. Britain is not a society racked by a recent history of social and political revolution. It is not surprising that we were less than vigilant. The values which spring from property seemed part of a timeless consensus. The political debate in the 1950s and 60s was about the extent to which socialist values could and should be accommodated. Socialism set the agenda, be it the political debate on the 'right mix' for the mixed economy or the merits of further nationalisation

Only during the 1974-1979 Labour Government was it finally grasped by much of the electorate that the ever-burgeoning growth of State power in the post-war years was infringing upon their liberties. Far from providing them with seemingly "free services" it was a very real interfering (and restrictive influence) in their daily lives.

Every Labour Government was acutely dependent upon the unions for the delivery of an industrial truce to stave off electoral defeat. When for the second time in ten years they failed to deliver and the country was thrown into the winter of discontent the electorate finally rejected the post-war consensus. 1979 was not merely a vote against union power,



it was vote against big bureaucracy, government interference. And it was by implication a vote for those things that would give the individual more liberty and responsibility:

- Property and particularly home ownership
- The rejection of nationalisation
- The need to reform the unions
- Lower taxation
- The control of public expenditure

The Conservative Party had been developing this message in the 1960s for it is a message which springs from our values. But when tested in 1974 the electorate was not ready finally to scrap the post-war consensus. The greatest achievement of the past seven years has been a decisive rejection of the resigned acceptance to nationalisation, to the growth in union power, to the diminution in the control in people's lives, to an ever larger proportion of taxation and public expenditure taken up by the the State.

The post-war consensus has been broken. Consolidating the changes we have put in place is our task for the next ten years. That work will be based on the same Conservative values that are behind policy today, the same values which underlay Conservative thinking in the '60s and earlier.

By looking at these threads <sup>18</sup> of continuity in Conservative



thinking we can draw up an agenda for the 1990s. First we can see that the spread of property ownership will become an explosion of capital and share ownership by much of the population.

Secondly, we shall develop policies to give people the freedom to spend more of their own money, not only for themselves but to enable them to exercise their own natural generosity. The reforms which we put through on Charitable Giving in the last Budget are a model of the kind of reforms which are integral to the kind of society Conservatives want to see.

Thirdly, we shall develop policies which encourage a sense of individual responsibility towards these very things<sup>for</sup> which Labour thinks only the State should be responsible. Should all the funds for State schools always come exclusively from the State? Property, freedom, responsibility, these words <sup>?</sup> betoken values on which much Conservative policy has been based. [a reference to Peel/Pitt the Younger?]

(Conservatives are not motivated by a burning ideology. The above policies will be implemented in a British way, with due respect to the traditions which have made Britain such a stable and pleasant place in which to live. They will be implemented gradually, with a proper scepticism for blueprints and plans.)

The aim of Conservative reform has been to contain the power of the State and to create a framework in which individual responsibility can flourish and prosper, economically as well



as spiritually. But new policies alone do not suffice. In 1979 the country badly needed a change in style and leadership, more honest and responsible, less dominated by political expediency.

The contribution of the Conservatives over the past seven years has been to provide fresh ideas and bold leadership. As De Tocqueville said:

"without ideas and leaders, a people cannot truly be said to exist."





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PPs - Rachel

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I'm not sure if

you saw an  
early version of  
this - 'V

will be press  
released thro'

CCO today

embargoed for  
about 2 pm - 2.30

Hegler  
16-7



*City. Just to be aware per**RL 16/2*

THE RT HON JOHN MACGREGOR OBE MP  
SPEAKING TO THE CROYDON SOUTH LADIES LUNCHEON CLUB  
ON WEDNESDAY, 16 JULY 1986

SAID:

The last thing Governments' could be accused of avoiding is reform the tax system - I am just entering the final lap of the 1986 Finance Bill - a mere 231 pages, 108 clauses and 22 schedules long - so far!

But there is one area where successive Governments have so far fought shy of reform - the tax treatment of husbands and wives. That is why in 1986, with a woman Prime Minister in her eighth year of office, successful women entrepreneurs creating jobs, women infiltrating boardrooms in the City and industrial firms we still have a tax system designed for the ladies of "Pride and Prejudice, whose sole aim in life was the making of a suitable match. The treatment of married women is little changed since 1805.

It is hardly any wonder that today's woman finds the way the tax system treats her bewildering and on occasion humiliating. Until she marries she is assumed capable of handling her own tax affairs, of filling in tax returns and of corresponding with the Inland Revenue. On marriage that capacity is deemed to disappear overnight. And with that the married woman loses every right to privacy. Her husband need not tell her how much he earns. But she must account to him for every penny in the Building Society or the Post Office.



That in itself makes a compelling case for the overhaul of our antique system. But the system itself seems positively to delight in producing perverse results.

Take, for example, the position of a young couple. Both work. The husband gets the married man's allowance. The wife gets her allowance equal to the single person's allowance. Together they have  $2\frac{1}{2}$  times the single allowance. They then decide to have a family. The wife decides to give up work to look after their baby. Their income goes down. But that is not the end of the financial squeeze. For they also lose the wife's earned income allowance. So at the time they face substantial extra outlays, the tax system turns the screw. But if the husband decided to stay at home they would have the same allowances as before. That can't be a sensible system.

Or take, for example, an elderly widow who marries again later in life. Her income from her modest savings is no longer offset against her tax allowance. Indeed it is added to her new husband's income - taxed as his, with no allowance. That can't be a sensible system.

That is why we have been determined to bite the bullet - and put the tax treatment of married and single people back onto the political agenda. The Green paper on Personal Taxation published at Budget time sets out an alternative system. A system which would

- treat married women as responsible adults in their own right;
- recognise the financial position of married couples with only one earner;
- remove the <sup>penalties on marriage</sup> incentives to stay unmarried;



We set out a system where if both partners are working they can enjoy full privacy. Their tax affairs would be completely independent. But it is a system which recognises the institution of marriage, and the dependency that can entail. Where a wife or a husband is dependent on their partner they can transfer their tax allowances to set against his or her income.

Our critics would prefer a system which did not recognise marriage at all. Marriage is more popular now that it was in Jane Austen's day. To fail to recognise marriage at all is simply to fail to take account of the reality of every day life. They would prefer to wean more people onto greater dependence on benefits - higher child benefit for instance. But that would not meet the needs of people who did not work for other reasons - to look after sick relatives or aged parents.

The Green Paper offers a way forward out of the present pre-Victorian absurdities. It deserves the support of all those Conservatives who care about the family and who care about the rights of wives and husbands.



FST'S SPEECH  
NEW DEVELOPMENTS IN  
VENTURE CAPITAL

2/7/86



fry

**FINANCIAL SECRETARY'S SPEECH TO THE CONFERENCE ON "NEW DEVELOPMENTS IN VENTURE CAPITAL" ON 2 JULY**

Introduction

1. You asked my predecessor at the Treasury, John Moore, to give the introductory talk for this conference on new developments in venture capital. This was a topic in which he took a close interest. And, from his experience of working in America, one to which he brought a particular expertise.  
[Something re Douglas French and Gloucester]
2. For my part however, I am particularly glad to have an opportunity so early after joining the Treasury team, of addressing a conference of the Venture Capital Industry.
3. You will have heard much from the Government about the great importance we place on bringing about an enterprise economy; and that this is essential for the creation of jobs. I regard the Venture Capital Industry as the cutting edge of that new approach.
4. So this audience is an extremely important group of people.
5. Our economy needs the partnership of those prepared to take risks both in running and financing business growth. The entrepreneurial spirit of those running a company and doing all they can to make it grow successfully has to be matched by a venture capital industry that is confident, vigorous and adventurous. The venture capital industry has developed in a very positive way in recent years and added a crucial impetus to successful business growth.



6. There is no doubt in my mind that the very fast growth of venture capital is one of the great success stories of the last few years, and one with enormous implications for the future.

7. I think it is true to say that when the Government took office 7 years ago, the UK venture capital industry scarcely existed.

8. The new companies which might have been expanding in the 1980's simply were not being formed, and who can blame managers for that? With a top earned income tax rate of 83% and an investment income surcharge of 15%, let alone CTT and an unindexed CGT regime, it is not surprising that potential entrepreneurs stayed in the warm embrace of their existing employers.

9. And this aversion to risk taking was also shown by the institutions, who would withdraw investment from a company at the first scent of trouble. In contrast, the venture capital funds will hang on, providing help and guidance.

10. The Government and the industry have worked together over the last seven years to bring about a transformation: the enthusiasm of the industry has been met by the Government's willingness to create an environment in which risk taking and enterprise can flourish.

11. Let us look in more detail at what we have achieved together.

12. There has been a dramatic rise in risk investment. There are now over 100 specialist venture capital funds in the UK, investing over £300 million in 1985.



13. In the past 3 years investments have been injected into about 2,000 companies - many of which were newly founded of the funds invested by UK funds in 1985, some £280m went into about 600 UK companies and almost  $\frac{1}{3}$  of these financings were for start ups or early stages of development. Venture capital also plays an important part in helping management buy-outs, where again there may be a degree of risk unattractive to more traditional institutional investors.

14. The areas of business covered by this investment are wide ranging. Consumer related industries, computers and electronics have from the start attracted large amounts. They continue to absorb about half the total investment.

15. But venture capital is not just about investors in electronics: there is an extensive list of other businesses including medical goods, industrial products communications and transport.

16. And beyond the figures I have given for investment by the specialist institutions are investments by non-specialist institutions and private placings by stock brokers both of them growth areas. Nor do they include direct BES investments by individuals.

17. And in the wider international context the British venture capital industry looks impressive. In terms of proportion of gross domestic product of the two countries, new investment in venture capital is now higher in Britain than in the US. This is a remarkable achievement given that the US has a history of over 20 years in venture capital.

18. A comparison with other European countries is at least as striking. A recent report shows that the UK now accounts for 43% of total venture capital raised in Europe, with the Netherlands a poor second at 18%.



19. It is important that we maintain this momentum. We need more new starts and more new businesses to respond quickly to the opportunities of changing markets.

New markets

20. One significant development is the response of the financial markets themselves to the change in the economic climate.

21. It is a little over five years since the Unlisted Securities Market was launched to stimulate the flow of new companies to the Stock Market.

22. The Market has had a remarkable growth. At the beginning of this year, the Market consisted of more than 340 companies with a combined worth of £b3.5. This year another 100 firms are expected to acquire USM status.

23. And since 1982, some eighty companies which started with venture capital have gone on to achieve a place on the USM or to a full Stock Exchange quotation.

24. In short, there now exists a continuous financing path, linking small equity injections from venture capitalists to full Stock Exchange listing.

25. And we will watch with interest the development of the third market on which over the counter issues can be more formally traded. This is a helpful development to make it easier for smaller businesses to raise equity and increase the total funds available.



What has the Government done to help bring this about?

26. The most significant achievement has, of course, been the success of our strategy in getting down inflation.

27. This was an essential condition for the revival of confidence and for economic recovery. Its undoubted success has led to a revival of investment and of new company formation.

28. In addition, we have removed a number of unnecessary controls - for example exchange controls, price and dividend controls - which prevented the free movement of capital.

29. We have also taken a number of measures to foster a more enterprise orientated economy, to encourage risk taking and kindle dynamism.

30. Income tax has been substantially reduced.

31. We have reduced corporation tax so that it is now at the lowest rate for any major country. We have reformed and simplified capital taxes.

32. But the most significant direct help provided by the Government is the Business Expansion Scheme, introduced in 1983. BES was highly innovative and it was seen very much as an experiment. So, up until this year's Budget, changes to the Scheme were kept to a minimum so that a proper assessment could be made.

33. Last autumn, the review of the scheme began, following completion of a report by Peat Marwick and the effectiveness of the Scheme in meeting its objectives.



34. This was against a background growing investment; over £105m in the first year, and at least £147m in over 787 companies in 1984/5. Last year's figures are not yet complete but we expect a further increase.

35. On the basis of that report and other evidence the Chancellor was sufficiently convinced of its success to give it a full lease of life. The extension has been widely welcome by all concerned with it.

36. Given this outlook, which has all Party support, and the acknowledged importance of the Scheme within the venture capital industry, I thought it would be useful to dwell a little on the changes that have been made this year.

#### Purpose of the Scheme

37. The purpose of the Scheme is to help small companies which are starting up or expanding to overcome the problem of obtaining sufficient equity capital.

38. Fifty years ago this problem was known as the "MacMillan gap". Today we call it the "equity gap".

39. The underlying aim of the Scheme is to help fill this gap and so promote new and expanded activity in the small companies sector. The Scheme therefore provides a very generous tax incentive to mobilise a new source of equity capital for small businesses.

40. The idea is to encourage individuals who are unconnected with a company, and who would not ordinarily invest in it - but who would put their savings in more conventional and safer savings vehicles - to take up new full risk equity of such a company on a reasonably long-term basis.



41. It is because of the risky nature of such an investment that the relief is so generous. So it is given, up front, at the investor's top rates of income tax.

42. Provided he holds the shares for at least five years, and the company continues to satisfy the conditions, this relief is retained. And now for shares issues after the Budget, any gains on disposals will also be free of capital gains tax.

43. Although the maximum investment is £40,000 in any one year, the average amount invested is about £4-5,000 with relief given at an average rate of about 50 per cent. So it is used by many more than just the highest rate taxpayers.

44. And as Peat Marwick found, 80 per cent of the investors they questioned had not previously invested in unquoted securities.

45. With such a generous relief it is important that it goes to the right places and does not get diverted to secure and less risky investment. For this reason the targeting has to be accurate, and the key changes this year were designed to improve this.

#### Target companies

46. BES is targeted on UK trading companies, and most trades are eligible across the manufacturing and service sectors.

47. In the first two years over one quarter of investment went into manufacturing, one eighth into wholesale and retail distribution, over two fifths into services, with the rest going to construction and other qualifying trades.



48. In less abstract terms investment went into everything from the latest information technology through manufacture of sports cars to local retail shops.

49. There are some exclusions - of essentially passive or financial operations - because these activities do not need this special incentive. But this line is extremely difficult to draw and changes have been necessary.

50. This year the changes we propose cut out of the Scheme companies trading in assets commonly held as investments or as collectors items and not actively trying to sell them. Also taken out were wholesalers who deal with other wholesalers rather than retailers.

51. These restrictions are designed to remove companies doing no more than investing in fine wine, art or antiques. But they should not affect the genuine trader such as the off licence.

52. The other main change was to restrict the extent to which companies with more than half their net assets in the form of land and buildings could qualify.

53. The purpose of this change is to ensure that an individual's investment cannot be largely safeguarded with low risk asset-based investment. This restriction will not apply to the first £50,000 the company raises in any 12 months.

54. Although this rule will be applied as simply and pragmatically as possible, it was thought that those seeking comparatively small amounts should not have to show they could satisfy the test.

55. There is one other important change regarding targeting. This concerns the new statutory instrument powers.



56. In the past, abuses of the Scheme have been cut out at Budget time. But in the run up to the Budget a great deal of investment has gone into projects which investors and promoters alike knew was outside the spirit of the Scheme.

57. The statutory instrument powers will allow changes to be made in the rules governing qualifying trades, and in the fraction of net assets that might be composed of land and buildings, without waiting for the Budget.

58. The response these powers confer means that promoters will have to think twice before putting forward the wrong sort of schemes. I am sorry to have to make the power sound so draconian, but anything less would be easily out-manoeuvred. However, I can assure promoters of schemes within the spirit that they have nothing to fear from these powers.

59. Not all the changes we have made have been restrictive. There are a number of general improvements for both investors and companies - the capital gains tax exemption and the relaxations in how groups might be eligible for example.

60. Many of these improvements were in response to suggestions made by those using the Scheme. Clearly we cannot pick up every justifiable point or deal with every anomaly without making the Scheme unduly complicated. But we think we have made the changes falling within the spirit of the Scheme which users most wanted.

61. I said earlier that I thought BES important to the venture capital industry. But BES depends too for its success on venture capitalists.

62. As Peats found, BES has done much to improve awareness and understanding in the small companies



sector of equity capital. More small companies now actively seek external equity finance, and are less reluctant to release a share of the business to outsiders. This means greater demand for venture capital services.

63. And of course BES has meant that investment in smaller amounts is nowadays a practical proposition. Although the larger BES deals have attracted most publicity, over 80 per cent of investments in the first two years were in amounts of £250,000 or less.

64. And companies have been coming back for more under the Scheme: 88 companies raised BES equity in both the first and second years.

65. Clearly BES is only one of the factors which has helped generate the recent growth in venture capital activity. But it is one factor the industry would do well to nurture further if it is to maintain and expand the pool of new and growing businesses using its services. For this reason venture capitalists are important to the future success of the Scheme.

66. The changes we have made to refocus the Scheme on the kind of risk investment for which it is intended means decisions will be more difficult for investors.

67. But venture capitalists can help here too: by presenting the opportunities clearly and putting them into perspective for the ordinary investor. This includes showing in a realistic way the genuinely high rewards that can be achieved.

68. It has often been said that part of the reason investors put their money in the kind of low risk asset-backed ventures we have seen is because these



are the very kind of businesses investors find easy to understand and so feel better placed to take investment decisions.

69. With the changes we have made it is all the more important investors not only get clear information about possible schemes, but that it is presented in such a way that they are likely to understand and grasp the opportunities.

Concluding remarks

70. The continued expansion of the venture capital market is of the highest importance for our economy.

71. I would like to see the investment figures I have quoted this morning multiplied 2, 4, tenfold.

72. And if only half the companies in which you invest are able to grow and employ new staff, imagine the effect on unemployment.

73. And this is not a short term solution, but a fundamental change.

74. But this is a high risk business, in which in the nature of things, there will be failures as well as successes. We naturally hope that there are more of the latter than of the former.

75. But, to get more new businesses we need more people with a vision of the future.

76. We have to build up amongst middle management a feeling that it is worth taking the risk of going



it alone. A recent survey carried out by the British Venture Capital Association indicated that a British manager is much less likely than his US counterpart to leave his company and take a risk.

77. We cannot judge for certain the impact of many of the changes encouraged by this Government but I believe that by the end of the century, many of the companies which have been created in recent years could be major forces in their markets and major employers of labour.

78. Much of the growth in employment in North America in recent years has come from the small technology company. A phenomenon we need to encourage in Britain. I noticed that Monday's Financial Times attributed Europe's weakness in computer technology to "the long standing reluctance of some larger electronics companies to accept commercial risk without lavish inducement from the public purse." Certainly we should not rely alone on the large company as a source of employment or innovation in advanced technology. We need to match America's entrepreneurs and venture capitalists to build tomorrow's industries and to employ the school leavers of the future.

79. Coming, as I do to this subject fairly recently, I look forward to hearing an account of the main points which emerge from this conference. I am sure that it will prove helpful in charting our future course.



MS1




28

FROM: A W KUCZYS  
DATE: 1 July 1986

PS/FINANCIAL SECRETARY

**FINANCIAL SECRETARY'S SPEECH TO THE WESTMINSTER AND CITY PROGRAMMES**

The Chancellor has seen the draft speech attached to your minute of 30 June, and commented "fine".

  
A W KUCZYS





PS/CHANCELLOR

FROM: VIVIEN LIFE

DATE: 30 June 1986

cc Mr Monck  
 Mr Scholar  
 Mr Monger  
 Miss O'Mara  
 Miss Sinclair  
 Mr Shaw  
 Mr Pickering  
 Mr Guy  
 Mr Haigh  
 Mr Ross-Goobey  
 Mr Cropper  
 Mr Beighton/IR  
 Mr Houghton/IR  
 Mr Reed/IR  
 Mr Bryce/IR  
 PS/IR

*Ch*  
 looks fairly standard.  
 Just drawing on your own  
 personal experience on the  
 subject.

*Content? (beamp  
 in mind FST will be taking  
 some more).*

*RL 3076*

**FINANCIAL SECRETARY'S SPEECH TO THE WESTMINSTER AND CITY PROGRAMMES**

I attach a draft of a speech which the Financial Secretary intends to give to the Conference on "New Developments in Venture Capital" on 2 July, being organised by Douglas French for "Westminster and City Programmes."

2. The Financial Secretary will be doing further work on this speech over-night: in the meantime I should be grateful to know if the Chancellor is content.

3. Separately, I should be grateful for further comments from copy addressees by 11.00 a.m. on 1 July. In particular, I am grateful to Mr Guy for his offer to check the figures on the growth <sup>of</sup> venture capital.

VIVIEN LIFE



**DRAFT SPEECH****FOR THE CONFERENCE ON "NEW DEVELOPMENTS IN VENTURE CAPITAL" ON 2 JULY****Introduction**

1. You asked my predecessor at the Treasury, John Moore, to give the introductory talk for this conference on new developments in venture capital. This was a topic in which he took a close interest. And, from his experience of working in America, one to which he brought a particular expertise.  
[Something re Douglas French and Gloucester]

2. For my part however, I am particularly glad to have an opportunity so early after joining the Treasury team, to have an opportunity of addressing a conference of the Venture Capital Industry.

3. You will have heard much from the Government about the great importance we place on bringing about an enterprise economy; and that this is essential for the creation of jobs. I regard the Venture Capital Industry as the cutting edge of that new approach.

4. So this audience is an extremely important group of people.

5. Our economy needs the partnership of those prepared to take risks both in running and financing business growth. The entrepreneurial spirit of those running a company and doing all they can to make it grow successfully has to be complemented by a venture capital industry that is confident, vigorous and adventurous. The venture capital industry has developed in a very positive way in recent years and added a

(Beef up)



crucial impetus to successful business growth.

6. There is no doubt in my mind that the rapid growth of venture capital is one of the great success stories of the last few years, and one with enormous benefits for the future.

~~What has brought this about?~~

7. I think it is true to say that when the Government took office 7 years ago, the UK venture capital industry scarcely existed.

8. The new companies which might have been expanding in the 1980's simply were not being formed, and who can blame managers for that? With a top earned income tax rate of 83% and an investment income surcharge of 15%, let alone CTT and an unindexed CGT regime, it is not surprising that potential entrepreneurs stayed in the warm embrace of their existing employers.

9. And this aversion to risk taking was also shown by the institutions, who would withdraw investment from a company at the first scent of trouble. In contrast, the venture capital funds will hang on, providing help and guidance.

10. The Government and the industry have worked together over the last seven years to bring about a transformation: the enthusiasm of the industry has been met by the Government's willingness to create a ~~tax~~ environment in which risk taking and enterprise can flourish.

11. Let us look in more detail at what we have achieved together.

12. There has been a dramatic rise in risk investment. There are now over 100 specialist venture capital funds,



investing over £300 million in 1985.

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14. The areas of business covered by this investment are wide ranging. Consumer related industries, computers and electronics have from the start attracted large amounts. They continue to absorb about half the total investment.

15. One such electronics firm is Microlec Limited who, following an injection of venture capital in 1983 went from breakeven to £1½m pre-tax profit.

16. But venture capital is not just about investors ~~in~~ electronics: there is an <sup>extensive</sup> ~~exclusive~~ list of other businesses including medical goods, industrial products communications and transport.

17. Another ~~successful~~ story is the Sterling Publishing Group, publishers of Business Year Books, who went from a loss to a pre-tax profit of £900,000 in 4 years.

18. And beyond the figures I have given for investment by the specialist institutions are investments by non-specialist institutions and private placings by stock brokers, both of them growth areas.



19. And in the wider international context the British venture capital industry looks impressive. In terms of proportion of gross domestic product of the two countries, new investment in venture capital is now higher in Britain than in the US. This is a remarkable achievement given that the US has a history of over 20 years in venture capital.

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What has the Government done to help bring this about?

~~First, inflation:~~

28. The most significant achievement has, of course, been the success of our strategy in ~~controlling~~ <sup>getting down</sup> inflation.

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~~Second~~

30. In addition, we have removed a number of unnecessary controls - for example exchange controls, price and dividend controls - which prevented the free movement of capital.

31. We have also taken a number of measures to foster a more enterprise orientated economy, to encourage risk taking and kindle dynamism.

32. Income tax has been substantially reduced.

33. We have reduced corporation tax so that it is now at the lowest rate for any major country. We have reformed and simplified capital taxes.

34. And we have cut, and substantially recast, stamp duty on shares which will in part help to bring dealing



costs in London into line with those in other international centres. // And it is not only the institutions which we wish to invest in small business. We want to encourage individuals to do so also.

35. We have therefore the new 'Personal Equity Plans' which will encourage direct investment in shares.

36. And we have the Business Expansion Scheme, introduced in 1983. BES was highly innovative and it was seen very much as an experiment. So, up until this year's Budget, changes to the Scheme were kept to a minimum so that a proper assessment could be made.

37. Last Autumn, the review of the scheme began, following completing<sup>ing</sup> of a report by Peat Marwick and the effectiveness of the Scheme in meeting its objectives.

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1



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69. Clearly BES is only one of the factors which has helped generate the recent growth in venture capital activity. But it is one factor the industry would do well to nurture further if it is to maintain and expand the pool of new and growing businesses using its services. For this reason venture capitalists are important to the future success of the Scheme.

70. The changes we have made to refocus the Scheme on the kind of risk investment for which it is intended means decisions will be more difficult for investors.

71. But venture capitalists can help here too: by presenting the opportunities clearly and putting them into perspective for the ordinary investor. This includes showing in a realistic way the genuinely high rewards that can be achieved.

72. It has often been said that part of the reason investors put their money in the kind of low risk asset-backed ventures we have seen is because these are the very kind of businesses investors find easy to understand and so feel better placed to take investment decisions.

73. With the changes we have made it is all the more important investors not only get clear information about possible schemes, but that it is presented in such a way that they are likely to understand and grasp the opportunities.



74. The continued expansion of the venture capital market is of the highest importance for our economy.

75. I would like to see the <sup>investment</sup> (figures I have quoted this morning multiplied 2, 4, tenfold.

76. And if only half the companies in which you invest employ one new person, imagine the effect on unemployment.

77. And this is not a short term ~~early~~ solution, but a fundamental change.

78. (By the end of the century, many of the companies which have been created in recent years will be major forces in their markets and major employers of labour.

79. But this is a high risk business, in which in the nature of things, there will be failures as well as successes. We naturally hope that there are more of the latter than of the former.

80. But, to get more new businesses we need more people with a vision of the future.

81. We have to build up amongst middle management a feeling that it is worth taking the risk of going it alone. A recent survey carried out by the British Venture Capital Association indicated that a British manager is much less likely than his US counterpart to leave his company and take a risk.

82. We need to change this view. And we need to educate the public how important risk takers are to the future of country's economy.

83. I hope we can build up a cult of praise for risk takers, for without them there will be no new businesses and no new industries to employ the school leavers of the future.



84. In particular, what I would like to see <sup>from</sup> the Venture Capital industries is a move to ~~spread~~ <sup>bring out</sup> them out in the regions. I know that it is in the regions where companies are having difficulty raising funds - there is general belief that both BES and the Venture capital industry ~~more~~ generally are too London based. I see one of the later <sup>Speakers</sup> ~~speeches~~ will be talking to you about a regional BES Funds.

85. As for what you would like from us, I know that those involved in the venture capital industry are seeking further direct tax incentives to, for example, encourage executives to set up in new high tech businesses.

86. And the specialist venture capital companies themselves are seeking a more favourable tax environment so that they can set up in the United Kingdom rather than, as at present, offshore.

87. We will give these proposals serious consideration.

88. Finally what I can assure you is that venture capital will not find a more supportive environment or Government than this one. The success of the venture capital industry in recent years is testimony to the vitality of the tradition of imagination, invention and entrepreneurship in this country.

89. It is important that this should not be stifled by a hostile tax and regulatory environment.

90. Coming, as I do to this subject fairly recently, I look forward to hearing an account of the main points which emerge from this conference. I am sure that it will prove helpful in charting our future course.



PWP



cc PS/Chancellor/2  
Sir Peter Middleton  
Mr F.E.R. Butler  
Mr Anson Mr Mowck  
Mr Turnbull  
Mr Gieve Mr Schuster  
Mr Towers Miss O'Mara  
Mr Tynia 12

MR CULPIN

CHIEF SECRETARY'S SPEECH

I attach the final version of the Chief Secretary's speech on Sunday, which Mr Tynia is arranging to be released from Conservative Central Office.

Jinluth

26.6.87



THE RT HON JOHN MAJOR MP FOR HUNTINGDON,  
CHIEF SECRETARY TO THE TREASURY,  
SPEAKING TO BUSINESSMEN IN HUNTINGDON

In the wake of the General Election there is a great deal of analysis to be done, for parties, pundits and pollsters alike. There were many factors which contributed to the outcome. First, it is striking that even after more than 8 years it is the party in Government which is bursting with new ideas and the Opposition which is intellectually bankrupt.

2. The thinking of the Labour Party has remained firmly rooted in the past. The lessons of the last 20 years have passed them by. But this should come as no surprise given its outdated structure, its antipathy to wealth creation and its instinctive sympathy for special interest groups rather than individuals.

3. The Conservative Party has been in the forefront in reappraising the the role of the state, in returning power to the consumer, in harnessing market forces, in promoting enterprise and wealth creation, and in spreading that wealth, whether in property or in financial assets as widely as possible through the community. We believe in ownership by the public rather than public ownership.

4. But on top of these trends in philosophy lay the immediate issues of the campaign. Labour took the only course it could, staking everything on promoting their leader in an effort to



avoid discussion of their policies. But this left them vulnerable to counter attack on the issues. The defence issue tolled heavily, killing their early momentum.

5. But as the campaign neared its close, it was the economic issues that came into prominence. Labour had tried to present their spending plans as part of a carefully costed and affordable programme. But good detective work soon blew that sky high. My predecessor costed their programme at £35 billion, a figure confirmed by independent analysts. Norman Fowler quickly showed that the social security proposals which were meant to cost £3½ billion would in fact cost over twice as much. And Nigel Lawson quickly discredited the claim that these plans could be financed while requiring not a penny more from those earning less than £25,000.

6. Labour laid claim to the moral high ground by arguing that higher public spending was justified and that people were prepared to pay for it. But they ceded that position when in their Manifesto they sought to hide the fact that higher taxes would be required across the whole income distribution, claiming their plans could be financed by soaking the rich. So what started as the politics of altruism descended into the politics of envy.

7. After Labour's defeat in 1983, Roy Hattersley put in his bid for the shadow Chancellorship by saying:

"Last month our economic policy ... was a net vote loser. Nobody believed that our theories would be put into practice. Our vague hopes of achieving growth through Government spending were barely understood and rarely believed."

The same was true again, only this time Labour tried harder, but in the end in vain, to hide the fact.

8. People have not forgotten that Labour Parties in office have resembled their recent election campaign - starting with a bang and ending with a whimper. It will not surprise you that the periods in which public spending has grown fastest were 1965-67 and 1974-75, in each case the start of a Labour Government. Within



two years in both cases the brakes were on, under international supervision.

9. The approach of this Government is precisely the opposite. We set before the people a programme based on sound finance, on reducing inflation, on the removal of controls and the promotion of enterprise and choice. We believe that the difficult decisions have to be taken first if the rewards are to be obtained. In our first term we had to give priority to bringing public borrowing under control. In our second term we were able to start to make progress in reducing the burden of taxation. By the end of our second term the economy had strengthened, taxes were down, borrowing was down, but resources for our priority programmes were up. And all this despite the loss of half our oil revenues.

10. What for me, coming to the Treasury, is the approach that I am going to adopt? The first theme must be continuity, sticking to the principles of sound finance which have served this country well over the past 8 years. I have not come in to find an economy in crisis which requires draconian action. But equally we must not let the growing strength of the economy delude us into thinking that restraint of public spending is unnecessary, for it was that restraint which has produced that strength.

11. I would summarise the principles we have followed as setting objectives, establishing priorities, value for money, and encouragement of choice.

12. We have sought to make a break from the practice of the '60s and '70s of building up public spending from the individual plans and then raising the taxes and borrowing to finance them. Plans were frequently over-ambitious and based on unrealistic expectation of the resources that would be available. So that when growth fell short the politicians first increased the burdens on the private sector in an effort to sustain their promises. But then they reneged on the promises themselves. No wonder public cynicism grew. Instead we have reversed the process, setting objectives for the finance that could be afforded, taking a cautious view of the prospects for the economy. And then we have constrained our spending plans within those limits.



13. And demanding objectives they are too. The Medium Term Financial Strategy sets out our intention to hold public borrowing to 1 per cent of national income and we have pledged in our Manifesto to reduce income tax to 25p in the pound.

14. Although we have been able to reduce taxes in each of the last five budgets, we cannot rest on that. We cannot be complacent about the levels of tax being paid by those on modest earnings. It cannot be right that a nurse earning say £155 a week should be paying around £41 a week in tax and contributions. Reducing taxation is part and parcel of the kind of society we want to see, where people retain more of what they earn, to spend or save as they choose, with the responsibilities that come with that freedom.

15. In order to reduce taxes and hold down borrowing it follows that we must stick to our objective of reducing public spending as a share of national income. We shall not allow ourselves to be deflected by any post-election euphoria from this task.

16. The growth of public spending in the 1960s and '70s averaged around 3 per cent in real terms - substantially in excess of the growth of the economy as a whole. We have brought the rate of growth down to less than half that, so that it is now substantially less than that of the economy as a whole. Since 1982-83 public spending as a proportion of national income has been reduced from 47 per cent to 43 per cent. This year will see a further fall and our plans imply a continuing reduction to around 41 per cent, which would be the lowest level since the early 1970s.

17. Within the limits we have set ourselves, we have been able to find resources to strengthen our priority programmes. We have greatly expanded the provision for training of young people, we have devoted substantial extra resources to law and order and to health, and education spending per pupil in real terms has risen by nearly a fifth. We have found the resources for this by cutting back unnecessary subsidies to industry, whether public or private sector; by giving greater responsibility to



the private sector for the provision of housing; and by cutting back excessive bureaucracy.

18. But we can continue to find resources for our priority programmes only if we subject all spending to rigorous scrutiny. We must continue to ask ourselves:

- what is this programme trying to achieve?
- Is it necessary, and if so does it need to be carried out in the public sector?
- Have clear and consistent objectives been set?
- Are performance targets demanding enough?

In short, it must be for those seeking public expenditure to justify the need rather than the reverse.

19. Our Manifesto contains many radical proposals, particularly for education, housing, and the regeneration of inner cities. But it will be clear from the Queen's Speech that there can be no blank cheques. This has never solved problems in the past and it will not in the future. The detailed plans in these areas will be subject to the same searching examination.

20. While the competition for resources remains so intense, the need for better value for money assumes greater and greater importance. I would like to pay tribute to my predecessor who did so much to bring value for money to the top of the agenda. At his insistence the debate is slowly switching from the money being put into programmes to the outputs being achieved. I certainly intend to keep up this pressure.

21. The benefits of the pursuit of value for money may not be as apparent as a new hospital or a new bypass, but let me assure you that its results are accumulating in an impressive way:

- £75 million improvements in Government purchasing;



- £140 million a year saving from contracting out;
- £400 million from the cost improvement programme of the health service
- we can now build four miles of motorway for the money which in 1978 would build only three.

22. Finally I singled out the theme of greater choice. For too long we have given excessive weight to the interests of the producers of public services and too little to those of the consumer. It is easy to understand why - the former are well organised and vocal, the latter are dispersed. But if we are to improve the standards of our public services we must harness this consumer interest. Our programme for the sale of council houses has transformed the position of over 1 million households. So in our proposals for education and housing we have put particular emphasis on the expansion of choice. Initially the numbers of children attending the new City Technology Colleges and the schools which opt to manage themselves under funding direct from Government may be small. But the knowledge that parents do have an alternative will have a powerful effect on the schools that remain with the local authorities.

23. No government finds control of public spending easy - there are always difficult choices to be made. And the forthcoming public expenditure Survey will be no different. But it is the hallmark of a strong government that it is able to face up to these choices. Furthermore, our experience over the past 8 years has illustrated the fact that if difficult decisions are faced up to the reward in terms of a stronger economy will be there. And this in turn will generate the resources for the improvement of our public services. But before you reap you must sow; and go on sowing.



FROM: ROBERT CULPIN  
DATE: 26 JUNE 1987

*Ruf*

MR TOWERS  
MR SEGAL

cc Chancellor  
Chief Secretary  
Sir P Middleton  
Mr F E R Butler  
Mr Turnbull  
Miss O'Mara  
Mr Pickford  
Mr Cropper  
Mr Tyrie

### CHIEF SECRETARY'S WEEKEND SPEECH ON PUBLIC EXPENDITURE

The Chief Secretary is delivering a substantial speech on Sunday: I will give you a copy separately. It is going out through Central Office; Mr Tyrie is drawing it to the attention of some Lobby journalists; and I will mention it to others. I should be grateful if you would point it out, as appropriate, to journalists with whom you are in contact over the weekend.

2. The speech will be released today under embargo for Sunday afternoon. It will be delivered at a fund-raising occasion in the Chief Secretary's constituency. It is aimed at Monday's papers.

3. It is Mr Major's first substantial speech in his new role. I hope you will encourage journalists to read it in full. The main Treasury message is clear:

- "We must not let the growing strength of the economy delude us into thinking that restraint of public expenditure is unnecessary, for it was that restraint which has produced that strength" (paragraph 10)
- "We shall stick to our objective of reducing public spending as a share of national income. We shall not allow ourselves to be deflected by any post-election euphoria from this task" (paragraph 15)
- "It will be clear from the Queen's Speech that there can be no blank cheques" (paragraph 19)



4. If you are asked where things stand on public expenditure, you should make two points:

i. spending this year is on track (so far as we can tell). See for example the published PSBR figures;

ii. the survey for future years has (quite obviously) barely started. We have no bids yet from the major spending departments.

5. You might keep in touch with Mr Tyrie, as appropriate, on 0277-840214 or 0277-841090.

A handwritten signature in black ink, consisting of a large, stylized capital letter 'R' with a small lowercase 'c' written below it.

**ROBERT CULPIN**



PWP



FROM: A P HUDSON

DATE: 25 June 1987

PS/CHIEF SECRETARY

cc: Mr F E R Butler  
Mr Turnbull  
Mr Culpin  
Mr Gieve  
Mr Tyrrie

## SPEECH ON PUBLIC SPENDING

This is to confirm the Chancellor's comments on the Chief Secretary's speech (on Mr Turnbull's 24 June), which I have already passed onto you.

2. The opening should not refer to the "tide of ideas", which the Chancellor will be speaking about himself in the Debate on the Address.

3. Paragraph 9 should say: "In our second term we were able to start to make progress in reducing the burden of taxation."

4. Paragraph 10: delete the sentence "I am not in the position of some previous holders of the office of Chief Secretary."

5. Paragraph 21 could quantify some of the benefits of the pursuit of value for money, eg getting four roads for the price of three.

6. In paragraph 22, the Chancellor suggests choosing an illustration other than the gas price ~~of~~ for the performance of privatised industry.

AHH

A P HUDSON



FROM: A TURNBULL  
DATE: 24 JUNE 1987

CHIEF SECRETARY

PS / Chancellor  
cc Mr F E R Butler  
Mr Culpin  
Mr Gieve  
Mr Tyrie

SPEECH ON PUBLIC SPENDING

I attach a further version of your speech which takes account of the drafting suggestions made at Tuesday's meeting. There are two gaps, both of which Mr Tyrie will be filling - the tax burdens on nurses and teachers, and the Hattersley quote.

AT

A TURNBULL

C

A few scribbled comments. No venue or time yet chosen.

~~AT~~



## DRAFT SPEECH FOR THE CHIEF SECRETARY

In the wake of the General Election there is a great deal of analysis to be done, for parties, pundits and pollsters alike. There were many factors which contributed to the outcome. A few <sup>weeks</sup> months ago the Chancellor said:

"No British Government has ever been defeated unless and until the tide of ideas has turned against it. And so far from turning, the tide of ideas that swept us into office in 1979 is flowing even more strongly today. And that, above all, is what will sweep us back into office on the 11th of June."

So indeed it proved to be. It is striking that even after more than 8 years it is the party in Government which is bursting with new ideas and the Opposition which is intellectually bankrupt.

2. The thinking of the Labour Party has remained firmly rooted in the past. The lessons of the last 20 years have passed them by. But this should come as no surprise given its outdated structure, its antipathy to wealth creation and its instinctive sympathy for special interest groups rather than individuals.

3. The Conservative Party has been in the forefront of the tide of new ideas which has been flowing both

X

You said this  
precise

[This last sentence,  
of course, came in  
Perth on 14 May.]



in Britain and throughout the rest of the industrial world; in reappraising the <sup>role of the</sup> state, in returning power to the consumer, in harnessing market forces, in promoting enterprise and wealth creation, and in spreading that wealth, whether in property or in financial assets <sup>shares or pensions</sup> as widely as possible through the community. We believe in ownership by the public rather than public ownership.

4. But on top of these trends in ideas and philosophy lay the immediate issues of the campaign. Labour took the only course it could, staking everything on promoting their leader in an effort to avoid discussion of their policies. But this left them vulnerable to counter attack on the issues. The defence issue tolled heavily, killing their early momentum.

5. But as the campaign neared its close, it was the economic issues that came into prominence. Labour had tried to present their spending plans as part of a carefully costed and affordable programme. But good detective work soon blew that sky high. My predecessor costed their programme at £35 billion, a figure confirmed by independent analysts. Norman Fowler quickly showed that the social security proposals which were meant to cost £3½ billion would in fact cost over twice as much. And Nigel Lawson quickly discredited the claim that these plans could be financed while requiring not a penny more from those earning less than £25,000.



6. Labour laid claim to the moral high ground by arguing that higher public spending was justified and that people were prepared to pay for it. But they ceded that position when in their Manifesto they sought to hide the fact that higher taxes would be required across the whole income distribution, claiming their plans could be financed by soaking the rich. So what started as the politics of altruism descended into the politics of envy.

7. In 1983 Roy Hattersley commented plaintively that:

To be continued

"We lost because our economic policies were not credible."

The same was true again, only this time Labour tried harder, but in the end in vain, to hide the fact.

8. People have not forgotten that Labour Parties in office have resembled their recent election campaign - starting with a bang and ending with a whimper. It will not surprise you that the periods in which public spending has grown fastest were 1965-67 and 1974-75, in each case the start of a Labour Government. Within two years in both cases the brakes were on, under international supervision.

9. The approach of this Government is precisely the opposite. We set before the people a programme based on sound finance, on reducing inflation, on the removal



of controls and the promotion of enterprise and choice. We believe that the difficult decisions have to be taken first if the rewards are to be obtained. In our first term we had to give priority to bringing public borrowing under control. In our second term we were able <sup>to start</sup> to make progress in reducing the burden of taxation. By the end of our second term the economy had strengthened, taxes were down, borrowing was down, but resources for our priority programmes were up. And all this despite the loss of half our oil revenues.

[Don't want to concede too much has been done here. Burden still higher than 1978-79, must come down.]

10. [What] for me, coming to the Treasury, [is the approach that I am going to adopt?] The first theme must be continuity, sticking to the principles of sound finance which have served this country well over the past 8 years. ~~[I am not in the position of some previous holders of the office of Chief Secretary.]~~ I have not come in to find an economy in crisis which requires draconian action. But equally we must not let the growing strength of the economy delude us into thinking that restraint of public spending is unnecessary, for it was <sup>precisely</sup> that restraint which [has] produced that strength.

Must not be interpreted as meaning P. Rees 1983!

11. I would summarise the principles we have followed as setting objectives, establishing priorities, value for money, and encouragement of choice.

12. We have sought to make a break from the practice of the '60s and '70s of building up public spending



from the individual plans and then raising the taxes and borrowing to finance them. Plans were frequently over-ambitious and based on unrealistic expectation of the resources that would be available. So that when growth fell short the politicians first increased the burdens on the private sector in an effort to sustain their promises. But then they reneged on the promises themselves. No wonder public cynicism grew. Instead we have reversed the process, setting **objectives** for the finance that could be afforded, taking a cautious view of the prospects for the economy. And then we have constrained our spending plans within those limits.

13. And demanding objectives they are too. The Medium Term Financial Strategy sets out our intention to hold public borrowing to 1 per cent of national income and we have pledged in our Manifesto to reduce income tax to 25p in the pound.

14. Although we have been able to reduce taxes in each of the last five budgets, we cannot rest on that. We cannot be complacent about the levels of tax being paid by those on modest earnings. It cannot be right that a staff nurse or a teacher earning say £x a year should be paying y per cent in tax. Reducing taxation is part and parcel of the kind of society we want to see, where people retain more of what they earn, to spend or save as they choose, with the responsibilities that come with that freedom.

Not complacent about  
the overall tax burden.



15. In order to reduce taxes and hold down borrowing it follows that we must stick to our **objective** of reducing public spending as a share of national income. We must not allow ourselves to be deflected by any post-election euphoria from this task.

16. The growth of public spending in the 1960s and '70s averaged around 3 per cent in real terms - substantially in excess of the growth of the economy as a whole. We have brought the rate of growth down to less than half that, so that it is now substantially less than that of the economy as a whole. Since 1982-83 public spending as a proportion of national income has been reduced from 47 per cent to 43 per cent. This year will see a further fall and our plans imply a continuing reduction to around 41 per cent, which would be the lowest level since the early 1970s.

17. Within the limits we have set ourselves, we have been able to find resources to strengthen our **priority programmes**. We have greatly expanded the provision for training of young people, we have devoted substantial extra resources to law and order and to health, and education spending per pupil in real terms has risen by nearly a fifth. We have found the resources for this by cutting back unnecessary subsidies to industry, whether public or private sector; by giving greater responsibility to the private sector for the provision of housing; and by cutting back excessive bureaucracy.



18. But we can continue to find resources for our priority programmes only if we subject all spending to rigorous scrutiny. We must continue to ask ourselves:

- what is this programme trying to achieve?

- Is it necessary, and if so does it need to be carried out in the public sector?

- Have clear and consistent objectives been set?

- Are performance targets demanding enough?

In short, it must be for those seeking public expenditure to justify the need rather than the reverse.

19. Our Manifesto contains many radical proposals, particularly for education, housing, and the regeneration of inner cities. But it will be clear from the Queen's Speech that there can be no blank cheques. This has never solved problems in the past and it will not in the future. The detailed plans in these areas will be subject to the same searching examination.

20. While the competition for resources remains so intense, the need for better **value for money** assumes greater and greater importance. I would like to pay tribute to my predecessor who did so much to bring value for money to the top of the agenda. At his insistence the debate is slowly switching from the



money being put into programmes to the outputs being achieved. I certainly intend to keep up this pressure.

21. The benefits of the pursuit of value for money may not be as apparent as a new hospital or a new bypass, but let me assure that its results are accumulating in an impressive way:

- £75 million improvements in Government purchasing ~~in 1985-86;~~

- £140 million a year saving from contracting out;

- £400 million from the cost improvement programme of the health service.

22. Finally I singled out the theme of greater choice. For too long we have given excessive weight to the interests of the producers <sup>of public services</sup> and too little to those of the consumer. It is easy to understand why - the former are well organised and vocal, the latter are dispersed. But if we are to improve the standards of our public services we must harness this consumer interest. Our programme for the sale of council houses has transformed the position of over 1 million households. The recent reduction in the price of gas is but one illustration of the way in which the performance of the former nationalised industries is being transformed. So in our proposals for education

*Sandy This  
says plays it down too  
much - it means we  
get more hospitals -  
more roads - the latter  
has been quantified - 4  
for the price of 3.*

*Not the best  
example? Check*



and housing we have put particular emphasis on the expansion of choice. Initially the numbers of children attending the new City Technology Colleges and the schools which opt to manage themselves under funding direct from Government may be small. But the knowledge that parents do have an alternative will have a powerful effect on the schools that remain with the local authorities.

*Should he say this  
of schools generally?*

23. No government finds control of public spending easy - there are always difficult choices to be made. And the forthcoming public expenditure Survey will be no different. But it is the hallmark of a strong government that it is able to face up to these choices. Furthermore, our experience over the past 8 years has illustrated the fact that if difficult decisions are faced up to the reward in terms of a stronger economy will be there. And this in turn will generate the resources for the improvement of our public services. But before you reap you must sow; and go on sowing.



PWP

FROM: A TURNBULL  
DATE: 22 JUNE 1987

CHIEF SECRETARY

cc PS/Chancellor  
Mr F E R Butler  
Mr Anson  
Mr Monck  
Mr Scholar  
Mr Gieve  
Mr Culpin  
Mr Tyrrie

*I have  
discussed  
with R. Culpin*

*[Handwritten initials]*

## DRAFT SPEECH

I attach a first draft for a speech as requested in Miss Rutter's minute of 19 June. It has a political introduction which could be used when delivered orally and a section on public expenditure which could be the basis of a press release.

2. The themes it seeks to get across are:
  - continuity with previous policies;
  - puncturing of post-election complacency;
  - need to take difficult decisions early with rewards to be secured later;
  - no exemption for Manifesto proposals from duty to provide value for money.
3. We are available if you wish to discuss this further.

C.

I think this is good stuff. A key question is how to get across the importance of tax reduction as a tenet of economic policy, rather than as a residual.

*[Handwritten signature]*

*[Handwritten signature: V. Brown]*

B A TURNBULL

*(somewhat overlate  
by Guardian story  
of yesterday's speed)*  
AA



**DRAFT SPEECH FOR THE CHIEF SECRETARY**

In the wake of the General Election there is a great deal of analysis to be done, for parties, pundits and pollsters alike. There were many factors which contributed to the outcome - a ringing endorsement of the record and policies of the Conservative Party.

A few months ago the Chancellor said:

"No party that has stayed abreast of the mainstream of ideas has lost an election."

So indeed it proved to be.

2. The thinking of the Labour Party has remained firmly rooted in the past. But this should come as no surprise given its origins in the trade union movement, its outdated structure, its antipathy to wealth creation and its instinctive sympathy for the interests of producers rather than consumers.

3. A tide of new ideas has been flowing both in Britain and throughout the rest of the industrial world. And the Conservative Party has been very much in the forefront in reappraising the role of the state, in returning power to the consumer, in harnessing market forces, in promoting enterprise and wealth creation, and in spreading that wealth, whether in property or in financial assets as widely as possible through the community.

*Not quite these words, I don't think.*



4. But on top of these trends in ideas and philosophy lay the immediate issues of the campaign. It was a mistake for Labour to stake so much on promoting its leader, leaving itself so vulnerable to counter attack on the issues. The defence issue tolled heavily, killing their early momentum.

5. But as the campaign neared its close, the economic issues came into prominence. Labour had tried to present their spending plans as part of a carefully costed and affordable programme. But good detective work soon blew that high. Norman Fowler quickly showed that the social security proposals which were meant to cost £3½ billion would in fact cost over twice as much. And Nigel Lawson quickly discredited the claim that these plans could be financed while requiring not a penny more from those earning less than £25,000.

*He had blown it apart in early 1986!*

6. In 1983 Roy Hattersley commented plaintively that:

"We lost because our economic policies were not credible."

The same was true again, only this time Labour tried harder, but in the end in vain, to hide the fact.

7. People have not forgotten that Labour Parties in office have resembled their recent election campaign - starting with a bang and ending with a whimper. It



will not surprise you that the periods in which public spending has grown fastest were 1965-67 and 1974-75, in each case the start of a Labour Government. Within two years in both cases the brakes were on, under international supervision.

7. The approach of this Government could not be more different. We set before the people a programme based on sound finance, on low inflation, on the removal of controls and the promotion of enterprise and choice. We believe that the difficult decisions have to be taken if the rewards are to be obtained. In our first term we had to give priority to bringing public borrowing under control. In our second term we were able to make progress in reducing the burden of taxation. By the end of our second term the economy had so strengthened that we were able to produce the hat-trick - lower taxes, lower borrowing and additional resources for our priority programmes. And all this despite the loss of half our oil revenues.

8. So looking ahead at the start of our third term, what are the themes I would like to pick out? The first is continuity. We will stick to the principles which have served this country so well over the past eight years, keeping the public finances on a sound basis and transforming the strength of the economy. I would summarise those principles as objectives, priorities, value for money and choice.



9. We have sought to make a break from the practice of the '60s and '70s of building up public spending from the individual plans and then raising the taxes and borrowing to finance them. Plans were frequently over-ambitious and based on unrealistic expectation of the resources that would be available. So that when growth fell short it was the private sector that took the rap. Instead we have reversed the process, setting **objectives** for the finance that could be afforded, taking a cautious view of the prospects for the economy. And then we have constrained our spending plans within those limits.

10. And demanding objectives they are too. The Medium Term Financial Strategy sets out our intention to hold public borrowing to 1 per cent of national income and we have pledged in our Manifesto to reduce income tax to 25p in the pound.

"...as and when prudent..."  
"prudent" clearly means  
no risks with borrowing  
& inflation. But we've  
~~not~~ <sup>not</sup> ~~explained~~ gone into  
the spending v. tax issue  
recently. This is  
important for this speech.

11. Although we have been able to reduce taxes in each of the last five budgets, we cannot rest on that. Much of the righteous indignation against cutting taxes has come from those already comfortably off - but we cannot be complacent about the levels of tax being paid by those who are less so. It cannot be right that a staff nurse or a teacher earning say £x a year should be paying y per cent in tax. Reducing taxation is part and parcel of the kind of society we want to see, where people retain more of what they earn, to spend or save as they choose, with the responsibilities that come with that freedom.



12. In order to reduce taxes and hold down borrowing it follows that we must stick to our **objective** of reducing public spending as a share of national income. We must not allow ourselves to be deflected by any post-election euphoria from this task.

13. The growth of public spending in the 1960s and '70s averaged around 3 per cent in real terms - substantially in excess of the growth of the economy as a whole. We have brought the rate of growth down to less than half that, so that it is now substantially less than that of the economy as a whole. Since 1982-83 public spending as a proportion of national income has been reduced from 47 per cent to 43 per cent. This year will see a further fall and our plans imply a continuing reduction to around 41 per cent, which would be the lowest level since the 1970s.

14. Within the limits we have set ourselves, we have been able to find resources to strengthen our **priority programmes**. We have greatly expanded the provision for training of young people, we have devoted substantial extra resources to law and order and to health, and education spending per pupil in real terms has risen by nearly a fifth. We have found the resources for this by cutting back unnecessary subsidies to industry, whether public or private sector; by giving greater responsibility to the private sector for the provision of housing; and by cutting back excessive bureaucracy.



15. But we can continue to find resources for our priority programmes only if we subject all spending to rigorous scrutiny. We must ask ourselves:

- what is this programme trying to achieve?
- Does this activity need to be carried out in the public sector?
- Have clear and consistent objectives been set?
- Are performance targets demanding enough?

16. Our Manifesto contains many radical proposals, particularly for education, housing, and the regeneration of inner cities. But even for these there can be no blank cheques. This has never solved problems in the past and it will not in the future. The detailed plans in these areas will be subject to the same searching examination.

17. While the competition for resources remains so intense, the need for better **value for money** assumes greater and greater importance. I would like to pay tribute to my predecessor who did so much to bring value for money to the top of the agenda. At his insistence the debate is slowly switching from the



money being put into programmes to the outputs being achieved. I certainly intend to keep up this pressure.

18. The benefits of the pursuit of value for money may not be as apparent as a new hospital or a new bypass, but let me assure <sup>you</sup> that its results are beginning to accumulate in an impressive way:

- fx million saving from contracting out;
- fy million saving from public purchasing;
- fz million from the cost improvement programme of the health service.

19. Finally I singled out the theme of greater **choice**. For too long we have given excessive weight to the interests of the producers and too little to those of the consumer. It is easy to understand why - the former are well organised and vocal, the latter are dispersed. But if we are to improve the standards of our public services we must harness this consumer interest. Our programme for the sale of council houses has transformed the position of over 1 million households. The recent reduction in the price of gas is but one illustration of the way in which the performance of the former nationalised industries is being transformed. So in our proposals for education and housing we have put particular emphasis on the expansion of choice. Initially the numbers of children



attending the new City Technology Colleges, and the schools which opt to manage themselves under funding direct from Government may be small. But the knowledge that parents do have an alternative will have a powerful effect on the schools that remain with the local authorities.

20. No government finds control of public spending easy - there are always difficult choices to be made. And the forthcoming public expenditure Survey will be no different. But it is the hallmark of a strong government that it is able to face up to these choices. Furthermore, our experience over the past 8 years has given us the confidence that if difficult decisions are faced up to the reward in terms of a stronger economy will be there. And this in turn will generate the resources for the improvement of our public services. But before you reap you must sow; and go on sowing.



CONFIDENTIAL



FROM: JILL RUTTER

DATE: 19 June 1987

1 Alex ✓  
2 Andrew ✓

Ruf

MR GIEVE

cc:  
 PS/Chancellor  
 Mr F E R Butler  
 Mr Anson  
 Mr Turnbull  
 Mr Culpin  
 Mr Scholar  
 Mr Tyrie

**PUBLIC EXPENDITURE**

The Chief Secretary discussed with you ~~in~~ his desire to make an early speech to start setting the climate for the coming public expenditure round. This would in large part be retrospective - emphasising the way in which firm control of public expenditure had contributed to the success of the Government's economic policy and its ability to meet its wider economic objectives.

2 The Chief Secretary would also wish to point to the way in which there had been switches of emphasis within the public expenditure aggregates.

3 The speech should obviously be done in a way which did not offer hostages to fortune.

(b) The Chief Secretary asked if you, together with Mr Turnbull, could prepare a brief synopsis for Monday night, which he could then discuss with you, Mr Culpin and Mr Tyrie. We will be in touch to set up such a meeting.

5 The Chief Secretary would aim to put this out as a short press release towards to the weekend.

JILL RUTTER

Private Secretary



CST -

PUBLIC FINANCE FOUNDATION

7/7/86



PPS 12/2

*[Handwritten signature]*



# H. M. TREASURY

Parliament Street, London SW1P 3AG, Press Office: 01-233 3415  
Telex: 262405

7 July 1986

**SPEECH BY THE CHIEF SECRETARY TO THE TREASURY, THE RT HON JOHN  
MACGREGOR, OBE TO THE PUBLIC FINANCE FOUNDATION**

Attached is an extract from the speech made today by the Chief Secretary to the Treasury, The Rt Hon John MacGregor MP, OBE, to the Public Finance Foundation Seminar "Getting Value for Money in Business and Government".

PRESS OFFICE  
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92/86



## NATIONALISED INDUSTRIES

The same stress on improving efficiency and getting better value for money has characterised our approach to the nationalised industries.

When we came to office in 1979, it was clear that nationalised industries were not performing as well as they should. An opinion poll at the time found that 65 per cent of the population thought that nationalised industries were less efficient than private companies. The skills were there in nationalised industries but objectives were confused and performance suffered. There was no sense of direction or purpose. There was too much outside interference in day-to-day management decisions. And this mattered.

The state industrial sector that we inherited accounted for over one-tenth of the UK's gross domestic product and one-seventh of the nation's annual total investment. The nation was not getting value for money from the substantial resources that had been invested in nationalised industries over the years, and customers were not getting value for money in terms of the service which the industries offered.

We developed two approaches to this problem. First, we decided that industries which were ready for privatisation should be returned to the private sector. Much has been said elsewhere about privatisation, and I do not intend to discuss this in detail today other than to say that the benefits which privatisation has brought in terms of increased efficiency and business performance seem to me to be quite self-evident quite apart from the beneficial effect that privatisation through employee share schemes and wider share ownership has had on the patterns of ownership in this country.

The second approach which is the one that I want to emphasise today, represents the other side of the coin from privatisation. We were determined to increase the



commercialisation and business performance of those industries remaining at least for the time being in the public sector. This was clearly necessary not just as an adjunct to privatisation but as an objective in its own right if value for money was to be obtained. We put a great deal of effort therefore into refining the framework under which nationalised industries operate. Through a combination of tightly-defined strategic objectives, better monitoring, tough financial targets and performance aims, and improved corporate planning procedures, and getting the right people for the job we have been markedly successful. The increased commercialisation that has resulted has benefited not just the public expenditure totals but also the industries themselves, their employees, and their customers. Those who work in the industries have good reason to feel satisfied with the progress that is being made in improving performance.

The effect on public expenditure totals has been impressive and is clearly seen if the performance of those industries remaining for the time being in the public sector is separated out from the others. In 1981-82, seven nationalised sectors - coal, electricity, the Post Office, steel, rail, shipbuilding, water - accounted for nearly £3½ billion of public expenditure. This year, the same seven are only expected to need just over £½ billion. An annual saving of £2½ billion has been made in five years.

This has reduced borrowing below what it would otherwise have been and released resources for other priorities. It has been done without cutting services and it demonstrates the rewards that can be obtained from sensible public expenditure control.

How have these savings been achieved? Let me give some examples from individual industries. Take the steel industry. Over the period 1979 to 1985, productivity rose 135% compared with 13% for the economy as a whole. Unit labour costs fell



by just under 9% compared with an increase of 46% for the economy as a whole. Costs and productivity are now superior to those in either Japan or West Germany and British Steel has moved into the black for the first time in ten years. Further improvements are forecast this year.

Similarly productivity in the Post Office has risen by 15% since 1981, nearly half as much again as the national average and labour costs have risen by almost 3 percentage points below those for the economy as a whole. There has been an emphasis on cost-cutting but not at the expense of maintaining services. In the three years to 1984-85, the Post Office has reduced its unit costs by 7.2 per cent and bettered the target that we set it.

The coal industry has experienced an outstanding recovery since the strike. Its results in 1985-86 are the best for seven years: record levels of production have been achieved in recent months with output at over 3 tonnes per man shift. There has been a 25% increase in productivity compared with the pre-strike level.

Labour productivity in the electricity supply industry went up on average 4½ per cent a year from 1981-82 to 1984-85.

How have these results been achieved? As I have already mentioned, I believe that management and workforce alike have responded to the objectives that we have set and the need to minimise the industries' calls on the Exchequer. Second, there has been increasing emphasis in recent years upon the need for commercial, result-orientated management. This has been seen in the importance that we have attached to the refinement of output and performance indicators and the setting not only of tough financial targets but also of tough targets for costs. Third, and perhaps most important, I believe that those who work in the industries have begun to appreciate the reality of the world in which they necessarily operate and the demands that this imposes. They are beginning to get the message that the customer comes first. In essence, without value for money, commercial enterprises cannot survive.



## MANAGING TO GET BETTER VALUE FOR MONEY

7 July 1986

Speech by the Chief Secretary to the Treasury, the Rt Hon John MacGregor MP, to the Public Finance Foundation Seminar "Getting Value For Money in Business and Government"

### 1. INTRODUCTION

1.1 I should like first to thank the Public Finance Foundation and Deloittes for giving me this opportunity to open your seminar. They have provided a forum for you to exchange views and experiences from a wide range of backgrounds. I am sure that it is useful to take these chances to stand back from day-to-day concerns to look at what you actually want to achieve.

1.2 It is no secret that we are embarking on the annual round of planning public expenditure. Bids for public expenditure - the inputs - make good headlines.

1.3 Less newsworthy are the outputs. Managing public expenditure never seems to catch the journalist's eye. That is a pity. Getting value for money is every bit as important as controlling how much is spent.

1.4 Your other speakers today will say how they have managed to get better value for money. They represent some of the biggest organisations - public and private - in the country. Each has seen at first hand what good management can deliver.

1.5 I shall not offer you more of the same. In giving the opening address I believe that you would expect me to range more widely. I want first to remind you why all of us should care about efficiency. Second, I want to look at how we can put more managers in a position where they have to care about value for money. Third, I want to offer some comments on the recipe for success in the public sector - and on how we can overcome the problems we still face.



## 2. A NATIONAL CHALLENGE

2.1 We have to start with why efficiency matters. The answer should be fairly obvious, that inefficiency affects us all. For the country to prosper we need successful businesses which win orders and create jobs, and <sup>we</sup> need efficient public services. We cannot say that our past record has been a shining example. Too often too few cared if costs went up, value for money went down, and we fell behind our competitors.

2.2 A not inconsiderable contribution to our now improving economic performance is the fact that we are overcoming these problems. But the challenge for both public and private sectors is still to provide the goods and services people want at a price they can afford. Managers everywhere have to strive to provide a more cost-efficient service.

2.3 You know that, as always, people are the key. They need to care about doing a good job. But that is not enough. They must think about what they are trying to achieve and why; what it costs; if it still needs to be done; and whether there is a better way of doing it.

2.4 I am keen that I and my Ministerial colleagues should focus more and more on these questions every time we discuss public spending. But concern to achieve maximum value for money should not just be confined to "the bosses". Everyone in the enterprise - private or public - must care.

2.5 "Managers" are not some small select band. We are all managers of resources - if only of our own time. At the end of the line we want all individuals to feel responsible for individual outputs, and think all the time about how to get more of them.

2.6 But how can that be achieved?



### 3. PRIVATE SECTOR

there

3.1 It is easier to see in the private sector. There/is an obvious bottom line. Everyone in a business should know that it is the customer who pays the wages, who produces the profits and who ultimately creates the job. Failure to give customers what they want at a price they are prepared to pay means that business will fail.

3.2 That, at least, is how it should work in theory. But in practice business can let things drift. Bad habits can be learnt in easy times, when profits come easily and its a seller's market. There then comes a nasty shock when times change, and customers begin to drift away.

3.3 Many firms, worldwide, have had to face these problems in recent years. Some could not adapt and did not survive.

3.4 Firms which prospered did so in many different ways. But the essential messages from successful companies include the following:-

- exist for your customers
- identify your key selling points
- talk to (and listen to) the people who work for you
- encourage individual commitment by setting targets and delegating authority
- know what you achieve with your money and watch especially your cash flow - in other words sound financial management.

3.5 The picture for the corporate sector is now looking much better, though we cannot let up - much still needs to be done. Net company profits (excluding the North Sea and British Telecom)



rose by 21 per cent between 1984 and 1985. Manufacturing productivity has grown by over 30 per cent since 1980 - an average of 5 per cent a year for 5 years. New businesses registered for VAT at a rate of 500 a week in the first half of the 80s - 550 a week in 1984.

3.6 Government has played its part by creating the right climate and framework, and in practical ways. Fewer and simplified taxes and more freely functioning markets are essential. They let well-managed firms flourish. Prudent economic and financial policies mean that we can now look forward to much lower inflation than we have been used to for a long time. That helps businesses plan for the future.

3.7 But we are a long way from getting the benefits in one vital area. That is pay.

3.8 In the 70s pay demands of 20, 25 and even 30 per cent were common. Management yielded. But real living standards hardly rose at all. We saw high pay rises to match high inflation.

3.9. We have come a long way since then. Yet increases in wages still outstrip increases in productivity. We have lower inflation than anyone who started work since the late 1960s can remember. Yet pay is still rising almost 3 times as fast. That is a recipe for the destruction not the creation of jobs.

3.10 German and Japanese competitors are just as keen to take advantage of lower prices for energy and raw materials. They are not saddling themselves with pay increases of over 7 per cent.

3.11 Employers and employees alike have to realise that a rise of 1 per cent would be enough to maintain living standards. We have to break away from the notion that anything less than 5 per cent is a joke. That is a hangover from the 70s this country cannot afford. Getting rid of it is the best thing we could do for job prospects.



#### 4. NATIONALISED INDUSTRIES

4.1 The same stress on improving efficiency and getting better value for money has characterised our approach to the nationalised industries.

4.2 When we came to office in 1979, it was clear that nationalised industries were not performing as well as they should. An opinion poll at the time found that 65 per cent of the population thought that nationalised industries were less efficient than private companies. The skills were there in nationalised industries but objectives were confused and performance suffered. There was no sense of direction or purpose. There was too much outside interference in day-to-day management decisions. And this mattered.

4.3 The state industrial sector that we inherited accounted for over one-tenth of the UK's gross domestic product and one-seventh of the nation's annual total investment. The nation was not getting value for money from the substantial resources that had been invested in nationalised industries over the years, and customers were not getting value for money in terms of the service which the industries offered.

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commercialisation and business performance of those industries remaining at least for the time being in the public sector. This was clearly necessary not just as an adjunct to privatisation but as an objective in its own right if value for money was to be obtained. We put a great deal of effort therefore into refining the framework under which nationalised industries operate. Through a combination of tightly-defined strategic objectives, better monitoring, tough financial targets and performance aims, and improved corporate planning procedures, and getting the right people for the job we have been markedly successful. The increased commercialisation that has resulted has benefited not just the public expenditure totals but also the industries themselves, their employees, and their customers. Those who work in the industries have good reason to feel satisfied with the progress that is being made in improving performance.

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4.12 How have these results been achieved? As I have already mentioned, I believe that management and workforce alike have responded to the objectives that we have set and the need to minimise the industries' calls on the Exchequer. Second, there has been increasing emphasis in recent years upon the need for commercial, result-orientated management. This has been seen in the importance that we have attached to the refinement of output and performance indicators and the setting not only of tough financial targets but also of tough targets for costs. Third, and perhaps most important, I believe that those who work in the industries have begun to appreciate the reality of the world in which they necessarily operate and the demands that this imposes. They are beginning to get the message that the customer comes first. In essence, without value for money, commercial enterprises cannot survive.



## 5. COMPETITIVE TENDERING

5.1 If we cannot move a whole organisation from the public to the private sector we can bring some of the same disciplines to bear by letting the private sector tender for jobs traditionally done by public servants. This is being done with what I hope will be increasing success. Since 1979 government departments have saved £20 million net a year from contracting out. Departments are under instruction to ensure that as much departmental work as possible is subject to competition and, more specifically, they are required to test the market for five specified services: cleaning, laundry, catering, security guarding and maintenance. Good progress has been made on cleaning, laundry, and maintenance and departments have drawn up plans to test most areas by April 1987 (catering by April 1988).

5.2 A multi-departmental review of competitive tendering in government departments led by the Efficiency Unit has in recent months been finding out how departments have applied our policy, the benefits they have gained and learning lessons for the future. The results of this review are expected to be made known in the near future.

5.3 In the NHS, health authorities have been required since October 1983 to put support services out to tender. The policy has so far yielded estimated annual savings of £52 million, in respect of just over half of these services and more savings can be expected this year.

5.4 The story on local authorities is less impressive. Total savings achieved through competitive tendering in recent years is estimated to have been around £20 million a year but the scope for contracting out is considerably higher than this. The authorities are required to go out to competitive tender for much of their building and maintenance work. While this policy appears to be having a significant effect on their cost



effectiveness in construction, highways and maintenance, the major effect has been to sharpen the cost effectiveness of in-house management rather than to achieve any major transfer of work to the private sector. Moreover the momentum of voluntary contracting out of services, eg refuse collection and street cleaning, appears to have faltered, with only two new refuse collection contracts reported in 1984-85 compared with 13 new contracts in 1982-83. A consultation paper was issued in February 1985 setting out proposals for extending competitive pressures to a further range of local authorities activities. If the planned proposals are fully implemented further savings of at least £200 million a year should be achievable.

5.5 We need to convince managers that competitive tendering helps them provide services, and benefits their customers. Any manager in the public sector should be willing to test by competition any activity. Sometimes it will be found that the private sector is the best buy. Sometimes it will be the in-house operation. But asking the question should be seen as a part of every manager's duty to look for better value for money.



## 6. MANAGEMENT IN PUBLIC SERVICES

6.1 We have also spent 7 years working for better management within the public services. The recipe for success is basically the same as for any organisation. But there is one difference - there is no clearcut bottom line. You cannot rely on profit or loss to tell you whether a service is good or bad. Services like defence, police and prisons are not a direct transaction between supplier and customer. That means we have to look for different measures of performance. The questions become what we are giving the people of this country for the taxpayer's money? Could we do more for the same cost or the same for less? How does this stand in comparison with other ways we could use the money? We have some answers. But we are nowhere near the end of longterm reforms of the way money and people are managed. And there is still a long agenda of specific initiatives and reviews.

### More expert management of resources

6.2 These include bringing a more expert, professional approach to complex tasks.

6.3 Take purchasing. Departments spend over £7 billion a year on buying things as varied as rulers, roads, buildings and ballpens. The people doing the buying need to do the job well.

6.4 Following a review by civil servants in 1984 a small unit with specially recruited private sector buyers is helping them do it better. They are working to a target of improvements worth £400 million a year by next year.

6.5 This target excludes defence goods and services bought by the MoD. There Mr Peter Levene has a separate target equivalent to an improvement worth £800 million a year.

6.6 Competition in procurement will help bring these benefits. In 1979-80 only 30 per cent by value of MoD's contracts were



let competitively. By 1984-85 the figure had reached 46 per cent. It has since jumped to 60 per cent in 1985-86. Just two of the contracts let in this way save £160 million compared with the previously estimated cost - enough to buy a squadron of Harriers.

### Efficiency scrutinies

6.7 Another way of asking the crucial questions about what we are getting for the taxpayer's money is an efficiency scrutiny. Since 1979 the scrutiny programme led first by Lord Rayner and now by Sir Robin Ibbs has led to savings of £300 million a year from government departments.

6.8 The scrutiny technique is now applied across a wide area. It supported the Jarratt review of universities; is used in the NHS; and is a tool of senior management who can follow the pattern even when the Efficiency Unit are not involved.

6.9 Most early scrutinies looked at administrative spending and particular operations. But the technique has also spread to look at policy and operations together.

### Policy reviews

6.10 There is nothing new in the concept of a policy review. There has to be some way to look at particular areas in greater detail than can be done in the annual planning round.

6.11 The key feature of a policy review or a scrutiny must be to ask the basic questions: What is the aim? Does it have to be done? Is there a better way of doing it? Can we provide the same service for less? More or a better quality service for the same?

6.12 It is wrong to see reviews as solely cost-cutting exercises, though there will often be cost savings. The scrutiny of the Community Programme was mainly concerned with making the scheme



more effective. The report on legal aid which was published on 27 June gives particular attention to the quality of advice available locally from various agencies.

6.13 Other major examples from recent years are the reviews of social security and regional industrial policy. They show why we cannot rely just on occasional scrutinies and reviews. In-depth reviews are necessarily selective because they require a special effort. They may find a policy has drifted off course, or has ploughed on regardless of changes in the outside world, or is not delivering what was originally intended, or is no longer a priority compared to other programmes. So we have to find ways to look at all policies and programmes, to keep on asking how they are performing and whether they are still relevant, and where spending best achieves our objectives.

#### Financial management initiative

6.14 Our financial management initiative pulls together ways to do this. They include better training, better use of expert advice where needed, and stronger links between performance and pay and promotion. But four broad developments will show how Ministers and officials are managing better.

##### a) Top management systems

6.15 First, Ministers and senior officials now have better management systems. When I was in the Ministry of Agriculture I had each year from my officials a strategic plan for the whole department. This MINIM (Ministerial Information in MAFF) evolved year to year and no doubt will change further. But the version produced in 1985 showed how each of our 62 programmes related to our overall aims; and set out the objectives of each programme and the resources they would use. This helped me to focus on what we were going to do with the resources available; ask about ways of doing more or different things; and make sure decisions on priorities were reflected in plans.



6.16 Other departments have similar arrangements - MINIS in the Department of the Environment, Customs and Excise Management Plan, Department of Transport's Departmental Plan, the Inland Revenue's Senior Management System, and so on. They have already proved their worth. What we need to do now is build stronger links from the top management reviews - upwards into the annual review of public spending and downwards into line managers' budgets within departments.

6.17 At the end of 1984 the Efficiency Unit published a report on consultancy, inspection and review services in departments. This points to ways these services (staff inspectors, management services, operational research staff and so on) can help individual managers make budgetary controls work - while still giving senior managers the means to assure themselves that they are working. The new arrangements for controlling running costs we introduced from 1986-87 should also help the development of budgets as the primary means of control. But Ministers and senior managers will still want to look at how resources are being used. So there will still be a need for services like staff inspection which last year achieved net savings of 1600 posts in the non-industrial civil service.

#### b) Budgeting

6.18 Each department has been working to develop budgeting as the main means of setting objectives, allocating resources and reviewing performance. But a recent piece of work across departments will help make this happen. The review of budgeting led by Tony Wilson, the head of the government accountancy service showed that budgeting had made people much more aware of their costs. Many had responded by taking the initiative to improve their performance. But the good practices needed to be made more widespread.

6.19 We are doing this. Each department has been asked to follow up four principles:



- all managers, from the top right through the management line, are responsible for setting budgets and challenging the budget proposals put to them
- budgets link with the Government's spending plans, and turn those plans into action
- budgets include output and performance indicators, with regular evaluation of what has been achieved
- senior managers organise work so as to make clear who is responsible for setting priorities, managing resources and reviewing performance.

I want to emphasise here the importance of including the measurement of achievement in budgeting.

6.20 Budgeting in this way will reinforce, and be reinforced by, value for money targets.

#### c) Value for money targets

6.21 Sir Robin Ibbs and the Efficiency Unit have encouraged Ministers and senior officials to use their top management systems to identify areas where improvements in value for money are required and set specific targets for better performance. In the absence of profit as a spur to and measure of success, explicit targets are an important key to continuous improvements.

6.22 The results so far are clear-cut and encouraging. Targets are set both to achieve savings and to achieve more within agreed resources. For example:

- by improved targetting which involved directing the available resources further away from a uniform visiting pattern towards the areas of greater revenue risk, Customs and Excise have met their target to increase the tax recovered by VAT control visits-tax properly due-by 7 per cent.



- regional health authorities cost improvement programme which has a target to find £150 million new cash-releasing improvements this year: that means more cash to spend on services to patients

- DES targets for removing surplus school places: 1,125,000 by 1987 with further targets for later years.

6.23 Targets are useful to Ministers and permanent secretaries in defining strategy and creating additional room for manoeuvre within it by getting better performance from available resources. They encourage everyone to try that bit harder. When people are asked to put up a target most tend naturally to say what can routinely be expected if everyone works hard. That is a good start. But it should be only the start for discussions leading to a target which is that much more ambitious and demanding - though still realistic and supported by those who will have to deliver it.

6.24 But the success of targets will depend on how they are treated by Parliament and the public. They rightly expect us to set our spending plans and then stick to them. Cash limits are meant to be absolute. But targets for performance are different. If they are to be sufficiently demanding they will sometimes be missed. You cannot cheat the laws of probability.

6.25 The danger then is that failure to achieve the target will be seen as bad management and those involved may fear that they will be exposed to criticism. It is the expectation of this criticism which leads managers to set more cautious, undemanding targets. We must make clear that they are not to be seen in that light.

6.26 The Public Accounts Committee and the other Departmental Select Committees will be particularly important in gaining Parliamentary interest and understanding. They must of course continue to ensure that standards of probity are maintained,



and evaluate the effectiveness and value for money the civil service achieves. But failure to achieve a demanding target is not failure to deliver value for money. Failure to set sufficiently challenging targets is more culpable. I hope and believe they will find we share a common interest in conveying this distinction because none of us want to destroy initiative and make the civil service more cautious. We want to ensure that demanding but realistic objectives are set and be ready to understand when they are not always achieved, if it is for good or understandable reasons.

#### (d.) Policy evaluation

6.27 Top management systems, budgeting and value for money targets apply to programmes as well as the administration and management of public services. This area is often that bit harder. Managing policies cannot be like private industry where success is measurable and generates its own resources.

6.28 But we are making much progress. Too often in the past policies were launched with no clear statement of what they were meant to achieve, no measurements of what they actually achieved, and no interest in evaluating whether what was achieved was right and still wanted.

6.29 We saw the results in the review of regional industrial policy. The objectives were not precise and up to date. Decisions were not linked to the cost-effectiveness of schemes. The cost-per-job was over £30,000. It then required a major review and step changes to bring about the policy we have now with clear objectives, quantified tests of cost-effectiveness in terms of cost-per-job, and systematic monitoring and evaluation.

6.30 Compare this with the Business Expansion Scheme. That was set up from the start with defined objectives, a timetable for decisions on its future, and means to both monitor progress



(from the Inland Revenue's statistics) and evaluate the results (with the help of the consultancy study published after the Budget).

6.31 Other examples are in the report published last year by the Financial Management Unit, in the public expenditure White Paper, and in the publications and reports listed in the bibliographies there. We need more specific targets like the London Docklands Development Corporation's to release sites for 2,000 new houses in 1986-87; more schemes like the YTS which tell you both the unit costs and how many of the young people go on to jobs or further training; and more spending which has a limited life, like the small engineering firms investment scheme, linked to achieving of objectives.

6.32 The lessons from this are that we need to define in advance precisely what a programme is meant to achieve and how its results will be monitored and evaluated. So we have now made it a general rule for new programmes and for policy reviews. Each should include a clear statement of what will be achieved, by when, at what cost, and how progress will be measured.

6.33 This will help. But it does not make it any easier to define precisely the objectives of a programme where there are complex and interlocking policies. Nor does it tell us how to measure the final outputs and performance of, say, defence and health spending where you cannot point to things you can count directly.

6.34 What it does do is keep all of us on our toes to do the best we can. For example the public expenditure White Paper published in January had over 1200 measures of output and performance. And I intend there should be more next year.



## 7. EXTERNAL ENCOURAGEMENT AND PRESSURE

7.1 To bring about this change will require a further change in attitudes to public spending in Parliament and the public. Top management systems, budgeting, value for money targets, and policy evaluation can all lead to the conclusion that it would make good sense to do less of something, or stop it all together. The wrench may be less than with an occasional policy review. But it is a fact of political life that the Minister and constituency MPs and the press will hear from the beneficiaries of the programme - hear loudly and long. You will not hear from all the taxpayers who have made the spending possible and might well think it was a good idea to stop it.

7.2 The trouble is that people got into the habit of measuring a spending programme by how much money was pumped into it. They thought of this not as their money, or the taxpayer's money, but as "public money". I almost said monopoly money because some people seem to think it is specially printed for them to play with.

7.3 We have to change this focus. The test should be how much are we spending and what are we getting for the money. We have made progress. We are setting out more clearly in our plans who will be spending what, where, why, and with what results. But still we hear too little about the full equation - about real increases in spending per pupil in schools or about the NHS finding cost improvements equivalent to spending an extra £1 billion since 1979. The media seem to find the subject too technical.

7.4 External auditors can help here as with value for money targets. I have mentioned in that context the NAO. It is now two years since the NAO was established with a wider remit to assess value for money. Inevitably relations between Government and NAO and PAC are sometimes adversarial. But we are allies in the search for efficiency. I also welcome the work of the



Audit Commission in this field. In less than three years it has identified opportunities for improved value for money totalling £1 billion. These would not be cuts. Many would be good housekeeping with no drop in services - eg £100-130 from energy conservation, £120-140 by better transport management, and £150-200 from better purchasing.

7.5 Some of these savings are being implemented. But more could be had. People should want to see them made, and make sure their councillors take notice of the Audit Commission's work. I do not know how many ratepayers hear about those recommendations and ask what their council is doing. I know I wish it was more.



## 8. CONCLUSION

8.1 I am conscious that I have neared the end of my comments and yet only mentioned a fraction of the initiatives underway in central government and with barely a mention of the NHS and other areas. But I can sum up briefly. The question we all face - whether businessmen or public servant - is how to make people realise that we have just got to improve our efficiency. It is not a threat to anyone who cares about the service. It is not boring. We are committed to it - and by we I mean not just the government but all the thousands of public servants who want to give the public the best they can from the resources available. That is what we are in the public service to do.

8.2 My personal ambition is that hard work, careful planning and sound financial management will become the watchwords for everyone - in the private sector, in local authorities and in central government. They may not make headlines. But we have got to do it.



FST's

Speech  
TO PARTY CONFERENCE

7/10/86



*al*

**FROM: VIVIEN LIFE**  
**DATE: 30 July 1986**

**MR GRIMSTONE**

cc **PS/Chancellor**  
Miss O'Mara  
Mr Pickering  
Mr Ross Goobey o/r  
Mr Tyrie  
Mr Cropper

**FINANCIAL SECRETARY'S SPEECH TO THE PARTY CONFERENCE**

1. The Financial Secretary has agreed to speak early at the Conference - the morning of Tuesday 7 October - on privatisation. I attach a copy of the motion. When Mr Ross-Goobey returns from leave I shall be asking him to draft a 15 minute speech. But in the meantime I should be most grateful if you could consider which points the speech might usefully contain so as to provide a basis for Alastair Ross-Goobey's work.

**VIVIEN LIFE**

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BIRMINGHAM YARDLEY CONSERVATIVE ASSOCIATION

"This Conference congratulates the Government on successfully transferring many manufacturing and service undertakings from deadening and restrictive state ownership to the healthier hands of private enterprise. It supports the continuation of this process but urges our Ministers to make much greater effort to explain the immense advantages this provides for all".





FROM: VIVIEN LIFE  
DATE: 19 August 1986

MR ROSS GOOBEY

cc PS/Chancellor  
Mrs Lomax  
Mr Ilett  
Miss O'Mara  
Mr Grimstone  
Mr Robson  
Mr Pickering  
Mr Hudson o/a  
Mr Tyrie  
Mr Cropper

### FINANCIAL SECRETARY'S SPEECH TO THE PARTY CONFERENCE

1. My minute of 30 July mentioned that I would be asking you to draft a 15 minutes speech for the Financial Secretary to make to the Party Conference and I attach for ease of reference a further copy of the motion. The Financial Secretary has asked for a number of factual points. I have minuted these separately to Mr Grimstone. He has also suggested the following points which he would like to make. He would like to:

- (i) demonstrate with concrete examples the advantage to the consumer of privatisation.
- (ii) demonstrate with concrete examples the importance we attach to competition, as well and what steps were actually taken to increase competition for British Telecom both in the appliances market and in relation to Mercury. He would like to spell this out in quite a lot of detail, the point being that the privatisation programme is not about creating private monopolies.
- (iii) spell out what is being done to get a better deal for the customer on gas and what is being done to increase competition here.



- (iv) look forward to the BGC privatisation. How many new shareholders do we expect to create?
- (v) deal with the argument: "what happens when the assets run out and that the Government is selling capital to finance current consumption ("family silver" arguments).
- (vi) argue that privatisation is now moving to a new chapter aimed at spreading ownership and place it in the context of personal equity plans, management buy-outs, pensions reform, council house sales etc and referring to new ways of buying and selling shares - Financial Services Bill Banks, Building Societies etc.
- (vii) refer to privatisation overseas. He would be grateful if you would look at the attached articles by Madson Pirie and from the Economist and let him know whether you think he could use any of this material. He would like to refer to privatisation in Pakistan, Bangladesh, Canada, Spain and France. He would be grateful for any information you may have about the size of the French Privatisation Programme.
- (viii) to refer to Labours' social ownership policy "Sounds like Nationalisation, smells like Nationalisation, feels like Nationalisation, is Nationalisation."

2. I should therefore be grateful if you could provide a draft speech by 5 September which includes these points and also indicates where the factual points requested in my minute to Mr Grimstone might be used.



VIVIEN LIFE



BIRMINGHAM YARDLEY CONSERVATIVE ASSOCIATION

"This Conference congratulates the Government on successfully transferring many manufacturing and service undertakings from deadening and restrictive state ownership to the healthier hands of private enterprise. It supports the continuation of this process but urges our Ministers to make much greater effort to explain the immense advantages this provides for all".



Privatization has become one of the world's growth industries. Governments everywhere — in the advanced economies, the Third World, even communist — are divesting themselves of state holdings and activities. Japan, having privatized its telecommunications system and launched its state tobacco and salt monopoly toward the private sector, has now embarked on the sale of Japan National Railways, which is to be broken up into six passenger and one freight company. This sale will dwarf that of Telecom, Britain's biggest to date.

Canada decided to sell its loss-making airframe makers, Canair and de Havilland, and Teleglobe Canada. Its privatization of the Canadian Arsenal, an arms manufacturing company, does not seem to have encountered the problems which led George Younger to delay the sale of the Royal Ordnance factories.

Britain could well be left behind by France, too, where a cohabiting Socialist president and right-wing premier are selling the TF1 public television station with an ease which puts Peacock to shame.

World Bank consultant Elliot Berg has identified 30 cases of divestiture of state-owned enterprises in Africa, not counting the privatization of Sasol, the oil-from-coal refineries in South Africa. He lists 165 examples from South America and 250 in Asia.

The cases are as diverse as the systems of government. Bangladesh has sold most of its jute, textile, chemical and engineering industries. Pakistan has privatized rural rice, cotton and flour mills.

In South American, democratic Mexico has privatized 73 of its 467 nationalized companies. Authoritarian Chile has sold 18 banks and 13 corporations, and turned its state pension system

## After John Moore's pledge to sell off all state undertakings, Madsen Pirie shows how privatization has swept the world

# British made —and exported everywhere

into a private sector operation. In the Pacific Basin, Korean Airlines and Singapore Airlines have already been floated, with the Malaysian Airlines System hard behind. All three countries are part way through massive programmes of divestiture.

Fidel Castro can hardly be accused of sharing Mrs Thatcher's motives. None the less, the sale of state houses to their tenants in Cuba, on the Thatcher model, has been a huge success. The same is true in China, with 6,000 flats in Shanghai alone passing last year into the private ownership of their former tenants.

Private food production in Hungary now accounts for half the total, and people are being invited to bid for the right to run state enterprises for profit. Meanwhile, across the Atlantic, the state and local governments of America are turning everything from bridges to prisons over to private, profit-making businesses.

The pattern is a bewildering one. A capitalist government in West Germany privatizes many of

the state banks and tourist offices. A communist government in China manages to get privately-owned restaurants and shops starting up at four times the rate of their state counterparts.

A military government in Chile sells shares in Chilectra, the state power company, and in the insurance companies which handle what was once state welfare. Meanwhile a democratic government in Brazil sells shares in Petrobras, the state oil company.

A country such as Sri Lanka, torn by civil strife, deregulates and privatizes its bus system, sells loss-making textile mills, and puts the telecommunications system up for sale.

Nominally socialist Spain sells SEAT, the national car manufacturer, while at the other end of Europe the rather more right-wing government of Turkey sells the Kevan hydro-electric dam and even the Bosphorus Bridge.

Not only do governments and economies vary, so do the methods and the motives. It might be by public floatation, as with

Singapore Airlines. It might be by private sale, as with Mexico's hotels. It might be a management-worker buyout, as with Britain's National Freight Corporation, or the use of private contractors, as with American prisons.

Some governments, like ours, do it inspired by a belief in free enterprise. These are comparatively rare. Many, like Bangladesh, do it because it works better, turning state loss makers into private, profitable and tax-paying enterprises. Some, like Sri Lanka, do it because the burden of the public sector is no longer tolerable. Privatization reduces the load on business and creates viable jobs where only subsidized ones existed.

Some, like Mexico and Brazil, do it to reduce national deficits. Privatized companies produce state revenues instead of consuming them. They enable state spending to be cut. Some, like Japan, do it because it makes for greater efficiency and because competition means better services and lower prices.

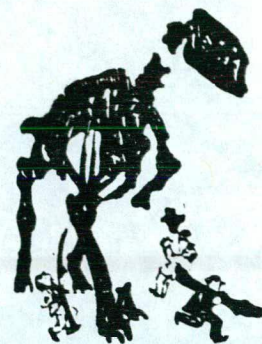
China and France do it to turn their countries around. South Korea and Singapore do it to keep them on course. There is no pattern and nowhere, except in Britain, is there yet a systematic policy. But the cumulative effect is overwhelming. After more than 100 years which saw the slow ascent to state activity and economic collectivism, the world is rushing back down that same slope at a dizzy, accelerating pace.

The world is turning private, and the policy machinery which is turning it that way was made in Britain, just as we made so much of the physical machinery of the first industrial revolution.

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The author is president of the Adam Smith Institute.





# Selling state fossils

State-owned fossils are being carted off into the private sector almost everywhere. Witness the denationalising of jute mills in Bangladesh and cotton mills in Pakistan; the bringing of France's nationalised giants to stock-market; the system of bidding for the right to run private businesses in communist Hungary, now spreading to its Comecon neighbours fast; the lowering of the state's share in Nippon Telegraph and Telephone, and the threat to split and sell the loss-making Japan National Railways; the promise to privatise Turkey's state airline and almost half of the 500-odd companies in Mexico's public sector; the list of sales in West Germany, Italy and Canada as well as the privatisation drive in Britain that we examine on pages 72-74. Mr Deng Xiaoping talks of "socialism with Chinese characteristics"; extraordinary things might happen if he lets a thousand Hongkongs bloom. In Moscow old apparatchiks fear that dangerously young Mr Gorbachev might give to markets some of their own privilege and power; modern Marxspeak for a privatisation drive is the "debate about economic reform".

Yet privatisation is not the philosopher's stone. The reasons governments give for selling off state assets are far less important than how they do it. Mrs Thatcher has found a dubious doctrine (that reduction of state power always increases the individual's freedom, wealth and happiness) where other privatisers seek pragmatism (state treasuries want to raise money without printing it). But privatisation will be judged a success only if the privately-owned British Telecoms or Montedisons or NTTs are more efficient. And, *pace* new zealots, privatised monopolies are not necessarily more efficient than nationalised ones. Ask Con Edison's blacked- and browned-out customers in New York.

None the less, the privatised concerns start with the advantage that most nationalised businesses are despised when they are not actually detested by their customers. In Britain, all trains do not run on time; major British Rail customers like British Steel believe they never will. The billions of taxpayers' dollars thrown at France's Renault, British Leyland and British coal very temporarily propped up thousands of rotten manual jobs, during a decade when America's unsubsidised small private businesses created 15m better ones at a fraction of the investment cost per worker. In Mexico, the only state firm to run a substantial profit is

the state-owned oil company; in Argentina even that manages (amazingly) to lose money. Turkey's public enterprises made net losses equal to 3.9% of gdp in 1977-79; the IMF rightly told it to start privatising fast.

If privatisation is to prove more durably popular than the nationalisations of postwar Britain—when Welsh miners sang triumphant hymns to greet the National Coal Board's vesting day—the privatisers will have to accept that cultural differences run deep. The entrepreneurial dynamism of America—and the pink slips, mobility and relentless profit seeking that go with it—will quickly alienate people if imported raw into more settled European countries and Japan. The distinguishing feature of the 15-35% of democracies' workers who are in the public sector is that they are often nine tenths trade-unionised, while under one fifth of private enterprise's workers now usually are. Huge profits are to be made by cutting the restrictive overmanning which this over-unionisation has left behind.

## Capitalists on the shopfloor

Privatisation's most popular political message is that workers should be given a big financial stake in the privatised firms, either through share ownership or profit sharing. Britain's National Freight Consortium (see pages 76-77) has shown that workers' capitalism can bring an astonishing rethinking of business strategies.

Reforming governments, from Mrs Thatcher's to Mr Deng's, should understand that the aim is not to privatise for its own sake, but to increase competition for the sake of the consumer—which the Thatcher government, by transforming British Telecom from public to private quasi-monopoly, did not sufficiently do. Problem: it may be both convenient and sensible to rate such services as water, gas and electricity as natural monopolies, because fragmenting them will not increase Mr Average Householder's choice one jot. Solution: try to get different bodies to run natural monopolies in different parts of the country, and encourage takeovers within a regulated system. The best way to regulate natural monopolies is to limit their price rises, so that to increase their profits they must improve their efficiency; you have got your price controls right if the best performer wants to buy the worst performer even while the controls last. The worst way to regulate is to insist on a rate of return. That leads





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FROM: VIVIEN LIFE  
DATE: 19 August 1986

MR GRIMSTONE

cc PS/Chancellor  
Mrs Lomax  
Mr Ilett  
Miss O'Mara  
Mr Pickering  
Mr Ross Goobey  
Mr Tyrie  
Mr Cropper  
Mr Hudson o/a

FACTUAL POINTS FOR THE FINANCIAL SECRETARY'S PARTY CONFERENCE  
SPEECH

1. My minute of 30 July asked you to consider factual points for the Financial Secretary's speech to the Party Conference on privatisation. He has been considering this himself and has now given me a list of facts which he would find helpful.
2. What he would like is an indication of the best fact in answer to each point in as clear and precise form as possible - ideally one sentence. I appreciate that much of this material is already contained in the privatisation briefing book and other previous notes from your Division. However, it would be very helpful if you could provide the information in the form in which he has asked.
3. The sequence of these questions is I realise slightly random but I think the Financial Secretary would prefer to have the answers follow his numbering so that he can refer back to his original manuscript list of questions from which I am working, and then work the facts into his speech.
4. I should be grateful if you could let this office have a reply by Friday 5 September. The points are as follows:

(i) The number of first time shareholders in British Telecom

(ii) The number of new shareholders since 1979



- (iii) The total number of individual shareholders and any estimates of the numbers who might be regarded as potentially prepared to buy shares.
- (iv) The number of individual shareholders in National Freight, Vickers, Jaguar, and British Telecom both applying for and still holding shares and the percentage of these who are employees.
- (v) Do we have estimates of the number of management buy-outs since 1979?
- (vi) How many share shops are there or have opened since 1979, has there been a change in the law here?
- (vii) What is the total number of employee share schemes and the best estimate of the growth in the number of these schemes since 1979?
- (viii) What is the total number of workers who own shares in privatised concerns?
- (ix) Facts on British Telecom's charges since privatisation. Has it followed a policy of favouring business customers at the expense of private customers?
- (x) A list of the companies to be sold which can be used publicly and the official line on the timing of these sales.
- (xi) The total figure so far for the value of assets' sales and individual figures for each financial year since 1979/80 to the end of the PES period.
- (xii) The official line on electricity.



- (xiii) Examples of improvements in privatised companies, both improvements in companies in anticipation of privatisation (eg BA - is that the most concrete example and are there other examples) and improvements after privatisation - is it true that all companies have performed better after privatisation? The Financial Secretary is worried in particular about ABP and wonders whether he could make the assertion that all quoted companies have performed better.
- (xiv) The number of new jobs at Jaguar. Any other examples of employment being increased - what about National Freight?
- (xv) The number of jobs transferred from the public to the private sector. What will it be when the current privatisation for this Parliament is complete? He notes that John Moore used 600,000 in one speech.
- (xvi) Example of increased investment. He knows that NFC doubled its investment.
- (xvii) What was the percentage of all shares owned directly and by institutions in 1979-83 and now?
- (xviii) What is the proportion of industry which was state owned in 1979, the figure for 1985/6 and when the programme is complete? Again he recalls this from John Moore's speeches.
- (xix) Have telephone charges been falling in real terms, were they rising in real terms pre-privatisation?
- (xx) Did ending National Buses near monopoly really lower fares, can we demonstrate it with figures, did it create new jobs?
- (xxi) What instructions or recommendations to the Trade Unions give members on buying shares in BT.



(xxii) Did John Moore say all state industries would be sold. If so, the Financial Secretary assumes he could repeat it.

(xxiii) How many individuals bought shares in Jaguar originally. How many individual shareholders are there today?

(xxiv) What is the average value of new shareholdings? He saw a figure of 4,000 quoted in a Sunday Telegraph article on 17 August.



VIVIEN LIFE



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**FINANCIAL SECRETARY SPEECH ON PEPS: WIDER  
SHARE OWNERSHIP**

**STOCK EXCHANGE/DAILY MAIL CONFERENCE FOR SMALL  
INVESTORS**

**"HOW TO MAKE MONEY ON THE STOCK MARKET"**

I am delighted to have this opportunity to address your conference and grateful to you for inviting me. You have certainly chosen an eyecatching - and mouthwatering - title. I wish I could stay longer and learn more.

This conference comes at a time when all eyes are focused on the Big Bang due in two weeks' time. The Big Bang will no doubt take its place in the catalogue of changes in the way markets operate, changes prompted by competition, by technological innovation, and by the increasingly international nature of markets that this has produced.

But what will all these changes mean for the small investor? I am glad your conference is seeking to answer this question. For it is vital that the small shareholder should have



a place in the sun in the new environment. Understandably this conference has concentrated on the benefits to the investor himself. But this Government believes that it is in the national interest, as well as in the individual interest, for small investors to get involved - and to make money - on the stock market. Wider share ownership means that:

- individual savings are channelled directly into British industry, with the market, not the Government, determining where the money can best be used.

- ordinary people can share in the profitability of UK industry, helping to destroy once and for all the myth that industrial profitability is somehow immoral.

- shareholders gain a greater understanding of how business works, and an understanding too, of the need for efficient, profitable companies, if the country as a whole is to prosper.

- employees, through employee share schemes, develop a much stronger sense of identification with their own companies.



## The Government's Contribution

For all these reasons, this Government has acted vigorously to encourage wider share ownership.

A key requirement was to restore investor confidence. Our policies have achieved the lowest level of inflation and the highest level of company profitability for a generation.

More specifically, we have made major changes to encourage the growth of employee share ownership. Six out of the last seven budgets have included measures in this area. We began in 1980 by making the existing profit sharing reliefs substantially more generous, notably by doubling the value of shares that could be allocated tax free. We also introduced a new tax relief for participants in savings related share option schemes. We improved the existing reliefs in 1982 and 1983, and in 1984 introduced a special tax regime for share option schemes.

The results have been dramatic. In 1979 there were only 30 all-employee share schemes. There are now over 1,100. And the figure is still growing. Something approaching



1½ million employees now have a stake in the firms they work for.

One of the main aims of our tax policy generally has been to reduce barriers and distortions on investment, including share ownership. We have reduced the rate of stamp duty on shares from 2% to ½%. The threshold for payment of capital gains tax has been increased almost six fold. The investment income surcharge has been abolished. And the Business Expansion Scheme has given a much needed boost to direct equity investment by individuals in small firms.

#### PRIVATISATION

The biggest boost so far to wider share ownership has been our privatisation programme.

Since 1979 twelve major companies have been returned to the free enterprise sector. This represents 400,000 employees and covers one fifth of the industry that the state owned in 1979.

Over 80% of the employees in those privatised companies became shareholders - one third of a million individual employees.



Experience has already shown that they made a wise decision. For example, the National Freight Consortium accounts for 1985 show that pre-tax profits increased by 70% on the previous year. Over the last five years there has been an increase of 600%; pre-tax profits in 1985 were over £28 million, 7 times the size of those in 1981, the year prior to privatisation. The value of employees' shares has increased 31-fold. No wonder employee morale is at a high level.

In terms of wider share ownership, the biggest success story so far has been British Telecom. There were over 2 million applications for shares, of which around 1 million were from new investors. Including employees and those holding shares jointly, there are still nearly 2 million BT shareholders.

Against this background we are planning to return another fifth of state owned industry to its rightful place in the private sector, by the end of next year. Next month British Gas will go on sale. This will be a mammoth issue of shares to out-strip even British Telecom. Next year British Airways, Rolls Royce and the British Airports Authority will be privatised and most of the remaining state owned industries will follow after the next



Election. Taken together these measures have succeeded in reversing the trend away from individual share ownership, a trend which in the 60's and 70's had looked inexorable. Estimates of the proportion of the population holding shares differ but it is common ground that the number holding shares has doubled since 1979. A survey commissioned by the Treasury suggested that one adult in seven now holds shares.

### Personal Equity Plan

This is a substantial achievement. But more needs to be done. And in this year's Budget the Chancellor made clear that the Government was going to make a further contribution.

That is why we introduced the Personal Equity Plan. Its purpose is to encourage direct investment in equities.

Let me tell you how the new scheme will work and why we are confident it will succeed.

Starting next January anyone over eighteen years of age who is resident in the UK will be able to put their savings into a new Personal Equity Plan.



Under this scheme individual investors can subscribe up to £2,400 a year or £200 a month and their money will be used to give them a direct holding in UK equities.

All reinvested dividends on the shares, and all capital gains made on them, will be entirely free of tax. The only condition is that the shares are held in the plan for a short qualifying period.

And the tax advantages have been specifically designed so that the longer the investor keeps his money in the plan, the greater the tax benefit he gets.

We have kept arrangements as straightforward as possible for investors, particularly new investors.

- It will be the plan manager, and not the investor, who will have to claim the tax relief.
- There will be no capital gains tax calculations
- There will be no need for the investor to keep any records for the Inland Revenue



- In fact, as long as the plan is kept intact during the qualifying period, there is no need for the investor to declare his PEP to the Revenue at all.

On the other hand, the scheme is designed to strengthen the link between the investor and the companies he invests in. All or a major part of the investment must be held directly in shares.

So the investor will be able to look in the financial pages at breakfast time and see how much his share are worth. He will receive copies of the companies' annual report and accounts. And he will have the opportunity to attend shareholders' meetings and exercise his right to a vote. He will, therefore, have a real say in the running of the company.

Personal Equity plans must and will be attractive to investors. But the success of the scheme will also depend on the plan managers who will provide the facilities for investing in this new venture.

That is why we gave potential plan managers the opportunity to tell us what they would like to see included in the scheme. And we



have listened carefully to what they have told us. The design of the scheme has greatly benefited from their comments.

Some of them wanted investors to be able to put all their plan money into unit or investment trusts. But this would not give the investor the direct stake in the success of specific companies, which we want to see. That is why we have restricted the amount of this sort of holding to £420 or 25% of the annual subscription, whichever is the higher.

The choice of shares in which to invest will be for the investor and his plan manager. They are free to invest in any ordinary shares in the UK companies listed on the UK Stock Market. In the light of the powerful arguments from the Stock Exchange we have also decided that UK ordinary shares on the second tier, the Unlisted Shares Market, will qualify. This will give an even greater choice of companies in which to invest.

There are many who also told us that our limits on cash in the first year of a plan were a problem. We have looked at this and decided to make a change.



I can now tell you that the only restriction on cash holdings in the year a plan is started will be the overall subscription limit of £2400.

This will allow greater flexibility in the early stages of a plan.

The importance of the PEP scheme can be gauged from the interest which has been shown in it by the many people who would like to become plan managers. These include small specialised dealers and major high street institutions alike. And we have made it possible for building societies to take part.

Already advertisements are appearing from prospective managers, seeking to interest old and new customers in their proposed plans.

We have deliberately avoided imposing rules on how managers will levy their charges. But we have made it clear that subscribers must be told exactly how their fees will be calculated. So competition for investors' money will be both keen and fair.

For many investors this will be their first introduction to the Stock Market.



Some will doubtless wish to choose for themselves the shares they wish to invest in.

But others may not wish to take such an active role.

Plan managers will be able to offer them experience and guidance in the form of a discretionary scheme. In this case the investor will leave the choice of initial investment and subsequent management of the portfolio to his manager.

I am confident from the interest shown so far that from January next year potential investors will have the choice of many different Personal Equity Plan schemes. And that this will result in a significant new boost to share ownership in this country.

To return to the theme of your Conference. Many people have in the past been discouraged from investing on the Stock Exchange by the tax they would have to pay, and the complications in making returns to the Revenue.

Now, through the PEP scheme, they will be able to keep what they make, and not even declare



it. It is difficult to think of a more effective measure than this or any Government could have introduced in support of your objective.

### CONCLUSION

So let me sum up my message to you today, in wishing your Conference every success. We are creating a society in which earners become owners. Where enterprise and responsibility flourish side by side. Where managers can share a sense of common interest and purpose with their work-force.

The old "them and us" attitude is fast going out of date. We in the Government have created a new appetite for share ownership among the British public.

The rest is up to you.



FST'S

Speech on PEP'S

STOCK EXCHANGE / DAILY MAIL

CONFERENCE  
FOR SMALL INVESTORS

13/10/86



FST'S

"Highflyers" (2)

15/7/88





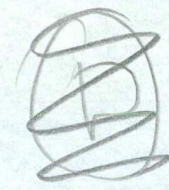
Inland Revenue

Policy Division  
Somerset House

FROM: A P HUDSON

DATE: 8 JULY 1986

APH



FINANCIAL SECRETARY

GREEN PAPER: SPEECH TO HIGHFLYERS' CONFERENCE, 15 JULY

1. I attach a draft speech for the Highflyers' Conference on 15 July. This incorporates comments from colleagues here and in the Treasury.
  
2. Much of the speech is an attack on mandatory separate taxation, focussing on the scheme put forward by the Institute for Fiscal Studies in their commentary on the Green Paper. I have tried to use this to illustate general points about MST. There is a clear risk that, by pointing out the defects of the present IFS scheme, we shall provoke them into devising a better one. Nonetheless, I think it is a risk we have to take at this stage. To try to regain the initiative in the public debate, we need to show two things: first, that MST does not have all the answers; and second, that the much-quoted IFS version has obvious shortcomings which have not so far been reported.
  
3. My advice, agreed with Mr Culpin and Ms Tyrrell, would be to press release the section on mandatory separate taxation beginning with the second and third sentences of paragraph 11, and including the first sentence of paragraph 12, and the whole of paragraphs 13 to 28 (omitting the reference to "chauvinism" in paragraph 25). This will focus journalists onto the new points you have to make.

cc Chancellor  
Mr Cassell  
Mr Monger  
Miss Sinclair  
Mr Culpin  
Mr Scotter  
Mr Cropper

Mr Isaac  
Mr Lewis  
Mr Mace  
Mr Hudson  
Ms Tyrrell  
Miss Murduck  
Mr Dodds

PS/IR



4. I attach also some briefing which may be helpful for the questions after the speech.
5. I shall be happy to help further, but am out of the office on Friday (11 July).

A handwritten signature consisting of the letters 'A', 'P', and 'H' in a stylized, cursive-like font, with a horizontal line crossing through the middle of the letters.

A P HUDSON



DRAFT SPEECH FOR FINANCIAL SECRETARY FOR HIGHFLYER'S  
CONFERENCE

1. It is three months to the day since my predecessor, John Moore, addressed the first of these Highflyers' Conferences in the Barbican. Since then, of course, John has been promoted to the Cabinet. I hope many of you will enjoy similar professional benefits from coming to the Conference.

2. Three months on, it is a good time to review the debate so far on the Green Paper, "The Reform of Personal Taxation", which was published on Budget Day. As with most subjects, some people have supported the Government's ideas, and others have been critical. I want to look at both sides of the argument.

The Present System

3. The present system of taxing husband and wife has been with us a long time. The principle of adding the incomes of a married couple together for tax purposes has applied since 1805, and the structure of the personal allowances has been the same since 1942: a married man gets an allowance which is  $1\frac{1}{2}$  times the single allowance; whereas a married women has an allowance equal to the single allowance, but which she can use only against her earnings.

4. It is not surprising that the practical results of a system this old are regarded by many as unacceptable.

Problems of the Present System

5. For a start, married women are not allowed to handle their own tax affairs. Many of you will have experienced this



problem. A married woman may be running a multi-million pound business, or may be a very senior solicitor or accountant, or may even be Prime Minister, but still has to conduct her tax affairs through her husband. This provokes a lot of complaints. A self-employed lady wrote in to say:

"My accounts are submitted by me in my name and accepted by the Inland Revenue in my name. Thereafter, however, all dealings are with my husband. I find it totally unacceptable, not to say insulting, that in the eyes of the Exchequer I am recognised as a person for taxation, but become non-existent when it comes to payment. Some time ago, I was informed that as far as the Inland Revenue was concerned, married women did not exist. My reply was to the effect that they could not have it both ways; if I didn't exist, I could not be expected to pay tax!"

Of course, if the problem were simply one of Inland Revenue procedures, it could be sorted out easily enough. But the problem is with the legislation - the Revenue are simply administering the law as it stands.

6. On top of these practical considerations, the present law can also mean that a married couple pay more tax than they would do if they lived together without marrying. This can happen for two reasons.

- First, a married woman does not have an allowance of her own to set against income from savings. This income is added to her husband's income, and the couple have to pay tax on it in full. If it outweighs the benefit of the married man's allowance, the couple will end up paying more tax between them than if they were both single.



- Second, married couples are also at a disadvantage in claiming some other reliefs and allowances. The most common example is mortgage interest relief, where two single people buying a house or flat can claim relief on up to £30,000 each, whereas a married couple only get £30,000 between them. I get a lot of letters about this too, many of them from worried parents, who think their children will succumb to the financial temptation not to get married!

7. The structure of personal allowances does not reflect the way married couples live their lives today. In the first half of this century, women usually gave up their jobs when they got married or had children, and rarely returned to the labour force. In 1931, for example, only 10.8 per cent of married women were out at work. Under these circumstances, the idea of a higher allowance for all married men, backed up by a special allowance where the wife did have earnings, may have seemed reasonable. But it is completely inappropriate today, when over 60% of married women are in the job market.

8. In many cases, when a couple marry, both will be out at work. But over the course of their married lives, they may each leave the labour force at different times and for different reasons: looking after children or other relatives; sickness; retraining or further study; or a spell of unemployment. But the present system is too rigid to take account of changes over the life cycle. When a couple are both in work, they get the equivalent of  $2\frac{1}{2}$  single allowances, and the same applies, curiously, when the wife is in work but the husband is not. But when the wife leaves paid work, the couple's allowances fall to  $1\frac{1}{2}$  times the single allowance. Of course, this typically happens when the couple have children for the first time. To take a simple example, a couple where the husband earns £8,000 and the wife £4,000 pay 14.5% of their income in tax. If the wife gives up work to have a child, the husband will pay



15.8% of his income in tax, and if he increases his earnings to £10,000, perhaps by working extra overtime, the proportion will go up to 18.4%. This is an unfair way of spreading the tax burden, and is one of the main reasons why married men supporting families are the largest single group in the poverty and unemployment traps.

#### The debate

9. In many ways, the biggest surprise is that the present system has survived so long. But if there were an easy way of solving all the problems, action would surely have been taken before now. Deciding what changes to make requires a judgment on some very complicated issues.

10. In spite of the way our political opponents present themselves as the apostles of equal opportunity, it has been Conservative Governments that have tackled these issues. A Conservative Government introduced the wife's earnings election in 1971, to reduce discrimination against working wives. The present Government renewed public debate on the issue with the 1980 Green Paper, "The Taxation of Husband and Wife". Having thought carefully about the responses to that Green Paper, we took the debate a stage further with the current one, published in March, which focusses on one possible way forward, independent taxation with transferable allowances. I should like now to look more closely at that approach, and some of the criticisms made of it.

#### The choice to be made

11. There is in fact a lot of common ground among people who have considered the issue. It seems agreed that the present system is unacceptable, and should be changed. And it seems agreed that the new system should be based on treating husband and wife as independent taxpayers, each with their own tax allowance, and each looking after their own tax affairs.



12. The question then is how to provide for couples where only one partner has income. These couples are not a fixed, unchanging group. Most couples will be a one-earner couple at some point during their married lives. At present, one-earner couples get at least  $1\frac{1}{2}$  single allowances, or  $2\frac{1}{2}$  if the wife is the breadwinner. Simply reducing all one-earner couples to one single allowance would make them all substantially worse off.

13. Two broad approaches having emerged, both based on giving a husband and wife an allowance equal to the single allowance. The Government's suggestion, outlined in the Green Paper, is that a married person who could not use up their own tax allowance should be able to transfer the balance to their partner. The alternative approach, which I will call mandatory separate taxation, is not really a taxation policy, but more a social security one. This approach also envisages giving each person a single allowance, but this could only be set against that person's own income. Where a partner in a marriage had little or no income, the couple could get no benefit from their allowance, and the other partner would pay tax in the same way as a single person. Under mandatory separate taxation, all one-earner couples would thus pay more tax than they do now, and to compensate for this, the advocates for MST<sup>1</sup> propose to increase social security benefits for people in particular circumstances.

14. There are fundamental differences between these two approaches. A different attitude to marriage: independent taxation with transferable allowances recognises not only the independence and equal status of partners within a marriage, but also the sharing of responsibilities, and the times when one partner is dependent on the other. Mandatory separate taxation, however, would ignore marriage altogether. And a different attitude to the State - should people keep more of their own money at times when they are supporting their husband or wife, or should the State collect more in taxation, so as to give it back in benefits?



## Examination of MST

15. Aside from these points of principle, let us look at the practicalities of mandatory separate taxation, or MST for short. Some newspaper reports suggest that it has all the answers and no drawbacks. Far from it, on closer inspection. The scheme that has been worked up in most detail so far is in the commentary on the Green Paper published by the Institute for Fiscal Studies at the end of May. This proposes a system of mandatory separate taxation, an increase in certain benefits, and a cut in the basic rate of tax to 25%. The IFS have designed the scheme to cost the same amount as they estimate transferable allowances would cost. So we can compare the IFS scheme directly with transferable allowances, against the criteria which the IFS themselves suggest.

16. The first of these is fairness. The "fairness" of particular schemes can be looked at in a number of ways. One point that seems agreed is that, to use the IFS's own words, "the principal unfairness in the (present) system is that two-earner couples are treated extremely well relative to their single-earner counterparts or to two single people". Transferable allowances tackle this problem directly, by raising the tax allowances for one-earner couples up to the level of those for two-earner couples. Thus, a married man supporting a young family on £150 a week would pay £13 a week less tax. Under the IFS scheme, he would pay more tax, but with higher child benefit would have a net gain of £2.85 if he had one child, or £8.85 if he had two. Contrast the married man on £150 a week whose wife is able to work, perhaps because their children are older, and who earns £100 a week. They would stay where they are under transferable allowances, whereas the IFS scheme would give them some £5 a week if they had one child or £11 if they had two.

17. One of the aims of most MST schemes is to direct more



resources to families with children. However, under this particular IFS scheme, one group who would lose out substantially to pay for the extra help for children would be pensioners. As a group, they would pay £400 million more tax! This is because many of today's pensioners are from a generation where it was much less common for married women to work, so they do not have pensions of their own. They are, in effect, one-earner couples. By contrast, transferable allowances fit the circumstances of pensioners rather well: all married women would have an allowance, so those with substantial pensions of their own would be treated as independent taxpayers; those with smaller pensions, perhaps based on their husband's contributions, would be able to transfer any unused allowances to their husbands. The great majority of taxpaying pensioners would be better off under transferable allowances, and pensioners as a group would pay the same share of the tax burden as they do now. But under any variant of MST, it seems inescapable that compensating pensioners for the loss of the married allowance would reduce considerably the money aimed at families with children.

18. The other main group who could stand to lose under MST are people who do not qualify for any of the benefits that would be increased. Examples include couples where one partner is unemployed, or studying, or retraining, or where, say, the wife has had to leave her job because her husband's job has moved to another part of the country. Transferable allowances have the flexibility to recognise all the circumstances in which one partner is dependent on the other. As the British Federation of University Women said in their evidence to a House of Lords Select Committee last year,



"We do not support any restriction on provision for the supported spouse. We do not accept that the Revenue Department ....

- or, presumably, the Government -

... has the right to designate the 'non-earning spouse' as the 'non-working spouse', nor to judge what constitutes specific home responsibilities, to the exclusion of other responsibilities such as community ones. Family circumstances vary between families and within families and with time."

19. One consequence of MST is that all married men would come into tax at a lower level of income. This has implications for the second criterion against which the IFS judge the schemes, the effect on the poverty trap. People find themselves in the poverty trap when, because of the combination of income tax, national insurance contributions, and the withdrawal of income-related benefits, they are little or no better off when their earnings increase. The amount they lose out of each extra pound of earnings is known as their marginal rate. On the IFS figures, 2.3% of heads of household would have marginal rates over 80% with current tax allowances. Their proposal for MST would increase the numbers of people affected by nearly 10%. Transferable allowances, however, would reduce the numbers by 70%, an important improvement in incentives for many married men with families. One of the key aims of transferable allowances is, of course, to direct more tax relief to this group.

20. A third criterion put forward by the IFS is neutrality to marriage - the idea that the tax system should neither favour marriage nor discriminate against it. On this basis transferable allowances have been criticised because they seek to take account of all the different circumstances of married couples whereas MST, it is alleged, is completely neutral towards marriage.



21. In practice there is no sensible way that the tax system can simply ignore marriage altogether. For example I think there are few who would suggest that inheritance tax should be neutral towards marriage - so that the transfer of the matrimonial home would be taxed when one marriage partner died. And it flies in the face of reality to imply that most married couples do not think about their financial arrangements together or that relationships between husband and wife are not rather closer than those between two people acting at arm's length! The tax system has to recognise that reality. [To take another example, who would pretend that a married couple do not have control of a company if the husband own 50% of the shares and the wife owns the other 50%] If marriage is a relevant factor in these other contexts, why should it be wrong to take it into account when working out a couple's income tax bill?

22. In fact, of course, the IFS themselves recognise that it is impossible to pretend that marriage does not exist. They say that MST would need to be coupled with a change in the rules to prevent husbands and wives covenanting income to each other in order to absorb unused personal allowances. But at that point the system ceases to be neutral towards marriage: it recognises marriage in order to discriminate against it.

23. A fourth criterion set out by the IFS is administration. We have always accepted that transferable allowances would require more computer support and more staff to run. This is not because the system is inherently complicated, but because it is flexible, giving couples the opportunity to transfer their allowances during the tax year to reflect changing circumstances as soon as possible. MST would not reflect a couple's circumstances so directly, so would be simpler to run, though there would be a lot more taxpayers.



24. The last criterion against which the IFS compare the schemes is work incentives for married women. Let me make clear that it is no part of the Government's intention to drive married women out of the labour force. As John Moore said in his speech three months ago, to suggest that that is our real aim is frankly verging on the offensive. Both transferable allowances and MST would give a working wife a full single allowance. The only difference is that under transferable allowances, a husband or wife would be able to make use of the allowance if their partner could not.

25. It has been argued that a husband who had got used to having both single allowances would resent his wife going back to work, because it could mean an increase in his own tax bill. Personally, I find it hard to believe that the men in this country are so chauvinist. Husbands in other countries which have transferable allowances do not seem to have behaved in this way. And there is, of course, already an element of transferability in the present UK system, where 340,000 wives are supporting their husbands and getting the married man's allowance transferred to them. I have not yet encountered a complaint from a husband that his wife will not let him go back to work because she is worried about her own tax bill increasing, irrespective of the effect on the family income.

26. I realise that some academic work has suggested that over 200,000 married women might give up work as a result of transferable allowances. I would not question the technical standard of the research, but I would like to put it in context. The economists in question are looking at the effect on the family's marginal rate of tax in isolation. They do not even allow for the value that married women set on an independent source of income - I cannot emphasise too often that the wife herself would not have to pay tax on the first pound of her earnings. And there are many other reasons why married women go out to work - companionship or interest, for example. Even leaving aside all this, the 200,000 women identified are



women working very short hours, on average under 5 hours a week. Married women working for periods as short as this are likely to be well below the present tax threshold, so their families would stand to gain considerably from transferable allowances.

### Conclusion

27. To sum up, MST emerges from the analysis as a system with a number of shortcomings. Most of these stem from the one fundamental flaw, that it ignores the way couples actually live their lives. Different couples spend varying periods in and out of employment, for different reasons. MST tries to ignore marriage and instead requires the State to decide which activities are socially worthwhile. By contrast, transferable allowances are a flexible system, which makes no value judgements but which can reflect the widely varying ways in which couples organise their lives.

28. There is a choice to be made, and one which needs to be made after careful consideration of all the arguments. I hope that as many people as possible will read the Green Paper, or a summary of it, and let us know their views.

[Reference to questionnaires, if any]



## WORK INCENTIVES FOR MARRIED WOMEN

### FACTUAL

#### Transferable Allowances

1. Under transferable allowances a wife will be able to earn up to the new single allowance before paying tax. Any unused allowance can be transferred to her husband but she can reclaim her allowance if she starts work or her earnings increase. Reclaiming her allowance would mean an increase in the husband's tax bill.

#### Numbers of working married women

2. The proportion of married women working or looking for work has been increasing (chart 2.2 of Green Paper).

Percentage of married women  
in labour market

1961	34.2
1971	48.9
1981	56.8
1984	62.4

#### Survey on Women in Employment

3. A survey 'European Women in Paid Employment 1984' conducted for the European Commission asked married women if they thought their country's tax system discouraged them from working. On average only 22 per cent thought that it did. In the UK the figure was 21% and in Denmark (which already has a system of transferable allowances) it was 22%.



## Criticism of transferable allowances

4. A frequent criticism of transferable allowances is that they would create a disincentive for married women to work.

Two reasons are usually given for this:

- a) If the husband is the only earner, under transferable allowances he will already be making full use of both his own and his wife's tax allowance (assuming she has transferred it to him while she is not in employment). If the wife wished to return to work, effectively all her income would be liable to tax because there would be no further tax allowance to set against their combined income.
- b) A husband who was enjoying the benefit of both his wife's and his own tax allowance would resent his wife going back to work, because when she claimed her allowance back from him, he would have to pay more tax.

## POSITIVE

1. No direct discrimination - a husband and wife are treated in exactly the same way under transferable allowances.
2. Transferable allowances will improve the incentive to work for husbands who are the sole earner in a family because they will enjoy higher tax allowances (2 single allowances compared to 1 under the present system) and so pay less tax. This will help alleviate the effects of the poverty and unemployment traps. One-earner families are the single largest group affected by the traps.



[Under the present tax system, married women already get both the married man's allowance and the wife's earned income allowance if they are the family breadwinner. So couples where the wife is the sole earner will not get any relative increase in allowances under transferable allowances].

### 3. European Survey on Women in Employment

(see factual 3)

Shows overwhelming majority of married women throughout the community do not believe the tax system in their country acts as a disincentive to work.

DEFENSIVE

#### Numbers of married women working

1. - The proportion of married women in work is increasing, not only in UK but throughout the European Community.

- This trend suggests that the increase is not being caused by any changes to tax systems or by any one specific tax system but for other reasons. (Tax systems range from aggregation in UK to income splitting in Germany and transferable allowances in Denmark.)

- Why should transferable allowances alter this trend? Wives will continue to have a single allowance to set against their income.

### 2. International Comparisons

- Denmark and Canada - which have systems similar to transferable allowances - have a relatively high proportion of married women in employment by international standards.



3. House of Lords Report [Select Committee on the European Communities 'Income Taxation and Equal Treatment for Men and Women' November 1985 HL 15]

(Evidence to this Committee by some economists suggests transferable allowances will act as a disincentive to married women working)

- the evidence is very theoretical, since it assumes a married woman's decision on whether or not to work is based only on the effect of marginal tax rates on the family income. But there are many other reasons why a woman chooses to work or stay at home. (independent income, companionship, etc.)

- Even so the results only suggest that women who work very short hours - an average of ~~one or~~ <sup>under five</sup> ~~two~~ a week - might be affected.

4. Answer to Criticisms

a) Wife's income taxed from first pound?

(see Factual 4 a)

Not how system will work. Wife will have her own single allowance. When she returns to work, she will reclaim this, and set it against her earnings. Any extra <sup>tax</sup> will fall on husband.  
h

b) Husband will resent wife returning to work?

(see Factual 4 b)

No evidence for this, and does not seem to be a problem abroad. Couples will soon get used to having one single allowance each, when both in work.



## PRIVACY

### Factual

1. Under the present tax system a wife's income is added to her husband's, and he is responsible in law for making a return of her income and paying the tax on it. In theory, a wife will therefore have no privacy because her husband will know how much income she has and its source, whether from earnings or investments, and how much tax is due on it. The wife on the other hand will know nothing about her husband's income or tax affairs except what he chooses to tell her. (This is mitigated in practice however, because the operation of PAYE means that for most working wives their tax is deducted at source and the majority of taxpayers are rarely required to submit a tax return.)

2. Under transferable allowances a husband and wife will be taxed independently. The husband will no longer be responsible for his wife's tax affairs. Each will submit their own tax return and pay their own tax.

3. A frequent criticism of transferable allowances is that if a wife transfers all or part of her tax allowance to her husband, he will then know the size of her income, so privacy is not guaranteed.

## POSITIVE

### 1. Equality

Under transferable allowances married women will be treated in all respects equally to married men. So they will both have an equal opportunity for privacy and independence.



2. Income above tax threshold

Married men and women with income above the tax threshold will be guaranteed privacy because they will not need to transfer any part of their tax allowance to their partner. They will at all times deal separately with the Inland Revenue.

DEFENSIVE

3. Income below tax threshold

Transferable allowances are flexible because there is a choice for married men or women with insufficient income to use any or all of their allowance.

- they can transfer the allowance to their partner and benefit from a lower tax bill. [In this case their partner will then know how much income they have, but not its source].
- or, if they want to ensure their complete privacy, they can decide not to transfer the allowance. [In this case full use will not be made of the allowance].



## PROGRAMME FOR IMPLEMENTATION OF TRANSFERABLE ALLOWANCES

### Factual

1. For operational reasons, TAs cannot start before the early 1990's. Whether a start is made then, and the period over which the change is phased, will depend on the amount of fiscal headroom at the time.

### Operational Considerations

2. a) Transferable allowances need computer support manual operation impossibly expensive, slow, and cumbersome.
- b) Computerisation of PAYE (COP) due to be completed and running by early 1988; computerisation of Schedule D (CODA) by 1989.
- c) In addition, transferable allowances need a data transmission network and index so that large amount of information can be passed quickly and efficiently between tax offices. These facilities can only be installed once basic computerisation is complete.
- d) Other essential job is to collect information to establish a link between records of husbands and wives. Present system only needs this link in a small minority of cases.

### Positive

#### 3. Computerisation

One of largest projects in Europe, implementation timetable remains on target. Gives UK an efficient and flexible way of running tax system.



Defensive

4. Can timetable be speeded up?

Satisfied that this is quickest feasible timetable. Depends on computer support becoming available.

5. What about the General Election between now and 1990?

Have to plan well in advance for any radical reform. If planning delayed until after General Election earliest introduction of transferable allowances, if Government decide to go ahead, could be put back until mid 1990's.

6. Why can no change at all be made before 1990?

What about disaggregation of married women's investment income?

Government will decide how to take reform of personal taxation forward in the light of the public response to the Green Paper.



## ADMINISTRATION OF TRANSFERABLE ALLOWANCES

### Factual

1. TAs would be a flexible system. Transfers of allowances would be given in tax codes before the start of the tax year, whenever possible. Requests for transfer during the tax year would be dealt with as soon as possible.
2. Aim would be to maintain present objective that most people pay right amount of tax during the year.
3. A criticism of transferable allowances (eg in the House of Lords Report) is that it would be complicated - both to understand and to administer.

### Positive

4. System in fact very simple in concept. Everybody starts with same allowance; sets it against their own income; any balance available for transfer if married.
5. No more need for taxpayers with income above threshold to make a return than under present system. Position of married people transferring allowances would be for consideration.

### Defensive

6. Complicated for taxpayers in practice?
  - No change for single people.
  - Simpler for couples where both partners have income above threshold (no aggregation or options for separate taxation).



- movements in prices and wages

- changes in tax rates and allowances in the period before transferable allowances were introduced.

b) Length of any phasing in period would also affect cost: revenue loss could be reduced if all or part of costs of indexation used to finance the change.



MISCELLANEOUS: POINTS MADE IN UNFAVOURABLE NEWSPAPER ARTICLES

DEFENSIVE

1. Green Paper fails to discuss workable alternatives to transferable allowances [M Prowse article 21 March, FT].

This has been done already: the 1980 Green Paper discussed a whole range of tax reforms including transferable allowances. This Green Paper takes the debate a stage further by concentrating on what is the Government's preferred option.

2. Transferable allowances will bring potential marital discord when a wife wishes to return to work and has to claim back her allowance [20 March, Guardian Leader].

Do not agree. Couples will soon be used to having one single allowance each. The element of transfer in the present system where the wife ~~as~~ breadwinner does not give rise to any complaints on this score.

3. Two earner couples have greater expenses and so less taxable capacity than one earner couples. They should get higher tax reliefs. [Fawcett Society letter 7 April, Times].

Two-earner couples have two incomes while the one-earner couple's single income must support two adults and in many cases children. These are the



families who represent the largest group affected by the poverty and unemployment traps. On transition to transferable allowances two-earner couples would keep same cash allowances; allowance for one-earner couples would be increased to that level.

4. Transferable allowances will be hideously complex to administer [M Prowse 29 May, FT]

Accept transferable allowances are not as simple as mandatory separate taxation (MST) but that is because it is a flexible system which will take account of changing circumstances over the life cycle.

MST is simple because it is a rigid system which cannot, of itself, cope with such changes.

Computerisation means that we are well able to have the the advantages of a flexible system.

5. Transferable allowances a plot to force women to stay at home and so help relieve the dole queues [Ann Segall 5 June, Daily Telegraph]

This is just arrant nonsense. The evidence is available for all to see: the number of married women working is on the increase throughout the European Community, irrespective of the type of tax system each country has to offer.

6. Total cost of Green Paper reform very expensive - about £5 billion [Lloyds Bank Economic Bulletin - April 1986]

a) As Green Paper explains, cannot give a single figure in isolation. Cost would depend upon a number of factors including



- Little change in practice for couples where only one partner has income.
  
- So only more complicated for couples (perhaps no more than 15 per cent of all tax units) where one partner has income below the threshold and is making a transfer. Even for these couples, system fairly straightforward except where circumstances change frequently making the right amount to transfer difficult to establish.

7. Changes to allowance for elderly, single parents could make the system simpler for them.

8. Complicated for the Revenue

Accept transferable allowances not as simple as some alternatives, but that is because it is a flexible system which will take account of changing circumstances over the life cycle. Computerisation means that we are well able to have the advantages of a flexible system.

9. Will require more staff

Annex 5 of the Green Paper says possibly several thousand extra staff might be necessary with a fully operational system. Well worth the cost for advantage of more flexible system.



CST'S

- 100 Club

16/7/86





# H. M. TREASURY

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## PLEASE NOTE EMBARGO

NOT FOR PUBLICATION, BROADCAST  
OR USE ON CLUB TAPES BEFORE  
2.30 PM ON MONDAY, 16 JUNE 1986

16 JUNE 1986

EXTRACT FROM A SPEECH BY THE RT HON JOHN MACGREGOR, OBE, MP, CHIEF  
SECRETARY TO THE TREASURY, TO THE 100 CLUB, ON 16 JUNE 1986

The vast improvement in Britain's economic performance is now being put at risk by one factor above all, excessive pay settlements, as today's report from the CBI reminds us.

The government's responsibility to industry is clear. It is to maintain sound money and free markets: to do what we can to promote an enterprise culture.

There is one thing this does not include. It is not the business of government to rescue industry from the consequences of excessive pay settlements.

If anyone doubts that currently they are excessive, let him look at the figures.

- Prices are rising at 2½% a year.
- Taxes are lower, so a pay rise of under 1% would be enough to compensate taxpayers for the last year's price increases.
- Yet pay is still rising at 7½%.

Governments in the past have let higher pay feed through to higher inflation. In one way or another, they have depreciated the currency.



We have refused, for seven years, to go down that road. We are not going to start now.

Each firm must judge its own situation for itself. Their competitive situation, their improvements in production and productivity will vary, so too therefore will their ability to pay. But in general, it is clear from the figures, across the board our managers are paying too much. And if they do, they can't look to us to bail them out.

Industrialists tell us that competition is tough, and indeed it is. But the remedy is in their own hands: it is to get a grip on costs.

If they rise so fast that our products are uncompetitive, the risks are obvious. People may spend their higher pay on goods from Japan and Germany rather than the UK. Profits will suffer. And we all know the inevitable result.

Economists estimate that every 1% on the level of real pay costs us between 110 thousand and 220 thousand jobs.

As managers think ahead to their next pay round, bear this in mind. We have honoured our commitment; we have secured a decisive fall in inflation. We now look to you, as managers, to secure a decisive fall in pay settlements.

PRESS OFFICE  
H M TREASURY  
PARLIAMENT STREET  
LONDON SW1 3AG

01-233 3415

85/86



47/48

*PPS*

FROM: ROBERT CULPIN

DATE: 16 JUNE 1986

MR PEGLER

cc PPS

Sir P Middleton

Mr F Butler

Mr Kemp

Mr Monck

Miss O'Mara

SPEECH FOR 100 GROUP: 16 JUNE 1986

Here, for the record, is the final version of the Chief Secretary's handout, which we are issuing this morning as a Treasury press notice.

*Rc*

ROBERT CULPIN

ENC



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**PRESS OFFICE  
H M TREASURY  
PARLIAMENT STREET  
LONDON SW1 3AG**

01-233 3415

85/86



Rachel

prop

Do you want to glance through  
this. Nothing else for us  
to do with it.

CR 16/2



MR PICKERING

cc PPS

Mr BURGER Mr CULPIN

Mr TURNBULL Mr GRIMSTONE

Mr TYRIE

CSI'S SPEECH AT 100 GROUP LUNCH

I attach (not proofread etc) a  
final draft of CSI's speech  
for today's lunch. Comments  
as quickly as possible please.

Paul Legler

16-6



SAID:

I hope I have said enough to show that things in Britain aren't what they used to be.

We have been in office seven years, which in the life of an economy and a society is not a long time.

Suppose, seven years ago, that I had come to this audience and told you this.

- That Britain would be enjoying steady, uninterrupted growth of around 3 per cent a year, for the longest period since the 1973 oil price shock.



- That we would move from the bottom to the top of the European growth league.
- That, in 1985, we would grow faster even than the United States.
- That, within that growth rate, investment and exports would rise at least as fast as consumption.
- That we would see a dramatic increase in our <sup>manufacturing</sup> productivity, with rises of over 3 per cent a year.
- That profitability in our companies is getting back to the levels of the early sixties - but we must do better still!
- That our current balance of payments would be in steady surplus, year after year.



- That this would be achieved not only with no resurgence of inflation but with a sustained fall.
  
- That we would have returned a fifth of the nationalised industries to the private sector with another fifth in the pipeline.
  
- And that we would have survived unscathed both a twelve-month coal strike and  
oil prices less than half their earlier level.

I wonder how many of you would have believed me then. Yet that is the record I report to you now - not as an aspiration but as an achievement.



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## CHIEF SECRETARY'S SPEECH TO 100 GROUP

Industrial Policy

It was suggested that I might talk about the Government's industrial policy. Delighted to do so.

2. Very often, as I go round the country, I meet people who tell me that they support what the Government is doing:

- to bring down inflation;
- to cut taxes;
- to remove controls;
- to promote new technology;
- to improve the curriculum in our schools and the training of our young people;
- to curb the excessive power of unions;
- to promote competition,

but then they say "if only the Government had an industrial strategy".

3. So I say, "what do you mean industrial strategy". Naturally accounts vary, but it usually goes something like this:

First, Government and industry should sit down together and agree what are the sectors of the future. Secondly, Government should be prepared to back the promising sectors with Government money. Finally, though this usually comes across a bit more obliquely, Government should be prepared to support the sectors in difficulties from overseas competition, by protection, subsidies or both.

4 Well, we did once have an industrial strategy pretty much like that in this country - the combination of picking winners and planning agreements of Denis Healey and Tony Benn, and the National Enterprise Board. Labour's industrial strategy gave



the unions a central role. From what we hear from Labour spokesmen today, the mixture is pretty much as before.

5 Labour have still not made up their minds whether they would still implement the policies they put forward in their 1983 manifesto. It is suggested the imposition of an extraordinary number of bureaucratic controls on industry; a new Department of Economic and Industrial Planning staffed by graduates from a new "National Planning College"; major companies required to formulate their development plans with the Government; a National Planning Council, superseding the NEDC, to establish committees to develop "strategies for the whole sectors of industry;" and a National Investment Bank.

6 We have to assume that much of this vast bureaucratic programme is still Labour policy. We now know that the National Investment Bank would be funded by taxing the pension funds. Repatriation of overseas

assets would be required under penalty of the removal of institutional tax privileges.

7 Recently John Smith Labour's Trade and Industry spokesman has also suggested the creation of a new organisation to be called, perhaps a little ironically, British Enterprise. This would be organised and funded by government - a kind of governmental venture capital organisation. It would be far the most determined attempt ever by a Labour Government to pick winners and second guess business decisions.

8 Planning would be Labour's watchword, As John Smith said in February:

"the responsibility for the central planning function must reside with the Secretary of State for the DTI".

But of course the unions would play a central role.

9 Labour shadow spokesmen are at pains to tell us that this time things would



be different. Last year Mr Hattersley said that he saw the need "for an agreement with the trade unions on everything" (Tribune 10 May 1985). He called it a compact. But changing the name from contract to compact does not change the policy or the philosophy. Mr Hattersley put it this way "a compact is different. It is offering (the unions) a new opportunity to take part in Government."

10 I believe Labour's industrial strategy would be wrecked by militants in the unions. But that is not the only or even the main reason why picking winners and central planning are inadequate. Let me explain why.

11. First, it was conceived largely in terms of large-scale manufacturing industry. It ignored the diversity of our industrial and commercial structure and the needs of small businesses. Above all it ignored the need to encourage the creation and development of small companies.

12. Secondly, it was extremely expensive - in terms of grants paid for large scale capital projects whose yield in terms of jobs was very small; and in terms of subsidies paid to loss-making industries.

13. Thirdly, most of this help went down a few throats - BL, British Steel, the aircraft industry - and was paid for by the many. In short, far from pick winners, it was a policy of taxing the profitable to finance the loss-makers.

14. But above all it was an industrial strategy that was totally flawed. For no strategy to promote industry can succeed when the rewards of success, ie profits, are disregarded.

15. No strategy to promote industry can succeed when the whole ethos of the society around it is antagonistic and when the Government promoting that strategy devalues the concepts of hard work, enterprise,



incentive reward and technological change.

16. But if the present Government does not have an industrial strategy of this kind, does this mean that we have no industrial strategy at all.

17. Far from it. The Government has a coherent strategy towards industry. And it is as much about what Government should do as what Government should not do.

18. Let me make it clear that the Government attaches the highest importance to a competitive, profitable and technologically advanced industrial sector. And when the Government talks about industry it does not mean simply manufacturing, though the health of that sector is vital. The Government wishes to promote industry and commerce across the whole spectrum whether manufacturing or services, whether exporting or serving the home market, whether larger or small. Our measure of success is not just winning a large export order in China or Korea but also the establishment of

three-thousand net new businesses a month.

19. It is essential that as a nation we place a higher value on industrial and commercial activity, that we recognise its crucial role in the process of creating the wealth on which better standards in our public services depend. How then do we go about achieving this?

20. First, we must recognise that it is for companies, and not Government to decide where the profitable opportunities lie and how they should be exploited. Companies, not second guessers in Whitehall, should take responsibility, and in turn must earn the rewards. This is indeed happening. The return earned by British industry has improved dramatically since 1981 and is now at the highest level since 1960 and the rate of corporation tax on those profits is now one of the lowest in the industrial world.

21. Secondly, we must remove unnecessary controls and regulations. This too is



happening. No longer do you have to ask Whitehall what prices you can charge or what dividends you pay, or where you invest your money. And bit by bit we are cutting through the jungle of regulations which small businesses in particular find such a burden.

22. Thirdly, we must increase competition and make markets work. Those of you from the City will be no stranger to this. New opportunities also are being opened up, for example, in the bus industry and in telecommunications. And we have just announced a review of existing policies on monopolies and restrictive practices.

23. Fourthly, we are building a better climate of industrial relations and encouraging greater flexibility of labour.

- by making unions accountable to their members and responsible in the use of their power;

- by giving more employees the chance to share in the profits of their enterprise.

- by removing obstacles in the labour market and easing wage rigidities.

24. Fifth, as part of our efforts to improve standards of education and training for our young people, we are placing more emphasis on giving them the skills and knowledge they will need in the real worlds and which you, as employers, have been calling for. Very big changes have been set in train. Let me give you just a few examples. The Youth Training Scheme, barely three years old, has provided more than 1 million school leavers with foundation training; and it is now being extended to give 2-years of high quality training to 16 year olds and 1-year to 17 year olds. The experimental Technical and Vocational Education Initiative is giving a tremendous stimulus to technical and vocational education for 14-18 year olds. The new GCSE exam will test practical skills; will raise standards of achievement; and will give employers a better idea of what candidates know and can do. These initiatives - and others too - will not



produce results overnight. But I believe that they will before very long transform the standards of vocational education and training in this country.

25. Sixthly, we are seeking to improve technology in this country not by backing a few prestige projects and hoping the benefits will trickle through the rest of the economy, but by promoting technologies and disseminating good practice which many sectors can use to advantage. We must stop labelling industries as sunset and sunrise, and ask how older industries can be transformed by the infusion of new technology.

26. Finally, and this is in large degree the responsibility of Government, industry needs a stable financial framework - a break from the past of boom and bust. This we have provided through tight control of public spending and borrowing. Our public finances have been robust enough to withstand the Falklands war, a year-

long miners' strike and the halving of oil prices. Inflation is at its lowest level for many years.

27. So when people say to me "where is the Government's industrial strategy?", I am reminded of Moliere's Monsieur Jourdain who discovered he had been talking prose all along. When one talks of the Government's economic policies, so too one has been talking all along about policies for promoting a strong and competitive private sector. In short, a policy for industry is not an extra to be bolted onto policies which are in other respects quite hostile to industry, but a thread which runs through the Government's policies as a whole.

28. These policies have major achievements to their name:

- better profits;
- increased productivity;
- fewer strikes;
- inflation at its lowest for years.



But an important challenge remains - that of unemployment. And this brings me back to pay for it is sharply rising unit costs that represents the Achilles heel of the British economy today. For you as Finance Directors it represents by far the biggest cost you have to meet - far greater than the level of interest or cost of raw materials, both of which have been falling. By contrast our unit labour costs rose by 5½ per cent in 1985. In contrast, US and France rose by 1½ per cent and Germany and Japan experienced no increase. It is this which must be reversed if we are to transform the prospects for jobs in this country.



SEPARATE SECTION TO BE  
SCOTTED IN AS APPROPRIATE

001/1284

Although I have focussed on the Government's industrial policy as it affects the private sector, it should not be forgotten that when we came to office in 1979, we inherited a sizeable State industrial sector that accounted for over one-tenth of the UK's Gross Domestic Product and one-seventh of the nation's annual total investment. Much has been said elsewhere about privatisation and I do not intend to discuss this in detail today other than to say that the benefits which privatisation has brought in terms of increased efficiency and business performance seem to me to be quite self-evident quite apart from the beneficial effect that privatisation through employee share schemes and wider share ownership has had on the patterns of ownership in this country.

But the other side of the coin is the great success that we have had in increasing the commercialisation



and business performance of those industries remaining at least for the time being in the public sector. This increased commercialisation has benefited not just the public expenditure totals but also the industries themselves, their employees and their customers.

Take the steel industry for example. Over the period from 1979 to 1985 productivity rose 135% compared with 13% for the economy as a whole. Labour costs fell by just over 9% compared with an increase of 46% for the economy as a whole. Costs and productivity are now superior to those in either Japan or West Germany and, as a result, British Steel has moved into the black for the first time in ten years.

Similarly productivity in the Post Office has risen 15% since 1981,



half as much again as the national average  
and labour costs have risen by 2% below  
those of the economy as a whole.



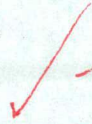
FROM: ROBERT CULPIN  
DATE: 13 JUNE 1986

CHIEF SECRETARY

*post*

cc Chancellor *e*  
Sir P Middleton  
Sir T Burns  
Mr F Butler  
Mr Kemp  
Mr Monck  
Mr Odling-Smee  
Mr Scholar  
Mr Turnbull  
Miss O'Mara  
Mr Pickford  
Mr Tryie

*Handwritten  
draft*



SPEECH FOR ONE HUNDRED GROUP: 16 JUNE

You asked for a handout on pay. Here is a draft.

ROBERT CULPIN

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OBE, MP, CHIEF SECRETARY TO THE TREASURY, TO THE  
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If you doubt that they are excessive, look at two figures.

**EITHER**

Prices are rising at 2¼% a year, pay at 7½%.

**OR**

A pay rise of under 1% would compensate taxpayers for price increases over the last year, yet pay is still rising at 7½%.

Governments in the past have let higher pay feed through to higher inflation. In one way or another, they have depreciated the currency.

We have refused, for seven years, to go down that road. We are not going to start now.

So if you, as managers, pay people too much, I tell you frankly that you can't look to us to bail you out.



Industrialists tell us that competition is tough, and indeed it is. But the remedy is in your own hands: it is to get a grip on costs.

If they rise so fast that your products are uncompetitive, the risks are obvious. People may spend their higher pay on goods from Japan and Germany rather than the UK. Profits will suffer. And we all know the inevitable result.

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CST's

INSTITUTE OF BANKERS

14/10/86



PWP



FROM: JILL RUTTER

DATE: 13 October 1986

MR ILETT

CC:

Principal Private Secretary  
 Financial Secretary  
 Economic Secretary  
 Sir Peter Middleton  
 Mr Cassell  
 Mrs Lomax  
 Mr Scholar  
 Mr Peretz  
 Mr Culpin  
 Mr M Hall  
 Mr C W Kelly  
 Miss O'Mara  
 Miss Sinclair  
 Mr Pickford  
 Mr Board  
 Mr Hudson  
 Mr Neilson  
 Mr Cropper  
 Mr Tyrie  
 Mr Ross Goobey

Ch  
 Notes remarkable ✓  
 AA  
 (but on market will be added tomorrow, depending on events).

CHIEF SECRETARY'S SPEECH TO THE INSTITUTE OF BANKERS,  
 NORWICH - 14 OCTOBER

... I attach a slightly amended version of the Chief Secretary's Speech. The Chief Secretary has decided against the Roskill press release.

2 I would be grateful for clearance by midday tomorrow.

JILL RUTTER

Private Secretary



THE RT HON JOHN MacGREGOR OBE MP  
SPEAKING TO THE INSTITUTE OF BANKERS - NORWICH  
ON TUESDAY, 14 OCTOBER

**Financial Services**

Norwich has a long association with the financial services industry. Members of the Institute of Bankers here tonight will not need me to remind them of the contribution which the banks and other financial institutions are making to the prosperity of East Anglia.

2 The banking sector is at the forefront of wide ranging and rapid changes.

3 Internationally, the major world markets are becoming one, drawn together by technology and competition. Much of the action is in the UK. The growth of international securities trading, both in equities and eurobonds, is phenomenal. Indeed, the traditional distinction between international banking and international securities has largely disappeared. Big Bang and the associated changes in the Stock Exchange reflect these developments and equip the City for the new world. The Government and the financial services industry have a common objective, to maintain and strengthen the UK's role as a leading world centre of great benefit to the UK economy.

4 I make no apology for dwelling on international aspect of the changing financial world. Nowhere are these more relevant to the domestic markets or to domestic concerns than in the United Kingdom.

5 Indeed, the forces which are making for change in the international markets have their parallel in the domestic market, in so far as one can distinguish the two.



6 Technological innovation has changed all our lives - not least yours - and is radically affecting the financial market place. Competition is increasing. The distinctions between traditional functions, traditional products and indeed traditional High Street institutions have diminished.

7 From 1 January next year, building societies will be free to compete with the retail banks in many more area. The banks have, of course, already made their mark in the building societies' traditional market.

8 And the conversion of the Trustees Savings Banks to their new status has added to competition in retail banking. And the TSB flotation has proved yet again the new found popularity of share ownership. Individuals who three of five years ago would never have dreamt of filling out a share application form are now old hands. The 3 million TSB shareholders join those with shares in British Aerospace, Jaguar and Telecom. Share-owning is becoming a habit. Up to 6 million people today own shares in British industry - double the number ub 1979. And one-quarter of those are employee shareholders.

#### **PEPs**

9 This year's Budget introduced a further measure designed to boost individual investment in shares. The Personal Equity Plan. This is designed to offer people incentives to make a regular commitment to share buying.

10 PEPs will provide the investor with an attractive means of buying equities up to £2,400 a year. Attractive in two ways. First, the investor will get income tax relief on dividends, provided these are kept within the plan. After



a short qualifying period of less than two years, he will get relief from any capital gains tax due if he sells his shares. Second, PEPs take the pain out of share buying. The Plan Manager will look after all the documentation and the investor will not need to have any contact with the Inland Revenue.

11 The role of the Plan Manager is clearly vital. So the Government has consulted potential plan managers at all stages in the preparation of the Regulations which will govern PEPs.

12 The banks have played a prominent and most constructive part in that process. Several major banks have already announced that they will offer personal Equity Plans to the public and I believe that others will follow. The Revenue have today published the draft regulations governing PEPs.

13 The banks' customer bases and branch networks put them in a position to make a very substantial contribution to the success of the scheme and indeed to wider share ownership generally. I look to you to grasp that opportunity.

#### **Prudential Matters**

14 But against the background of these positive developments a note of warning. We have seen increased competition in every aspect of deposit taking, lending and financial services. I welcome these developments, and I believe that the financial sector, its customers and the economy generally have benefited from them. But we need to make sure that the control mechanism fit the changed environment.

15 We have taken steps to ensure to bring the regulatory framework up-to date - to ensure that it can cope with the new pressures.

16 The Financial Services Bill which is now completing its passage through Parliament, will modernise and extend



the regulatory framework for investment. The Building Societies Act has updated the regulatory system for building societies. We have announced plans to strengthen banking supervision. And we are developing techniques and systems for the complex task of regulating financial conglomerates which are subject to more than one prudential regime.

17 But external regulation cannot be a substitute for self-regulation. I have no doubt of the benefit that increased competition can bring. I have no wish to return to the days of cosy cartels. But those responsible in banks and building societies for lending to the public must retain a degree of self-restraint. Expanding market share is a legitimate objective. But not at the expense of individuals who take on commitments they cannot sustain. We need to strike a sensible balance - to have responsible or prudent competition. Ultimately competition will work itself out - but we must not forget the human casualties - individuals who see their homes repossessed because they cannot afford the repayments on their mortgages, small businessmen who over-extend themselves.

18 The image and the success of the financial services industry relies on your own high professional standards. They should not be sacrificed in the pursuit of quick profits. The Institute has a key role to play in ensuring those standards are maintained.

### Fraud

19 But nothing can tarnish the image of the City, of the financial services industry, more rapidly or more devastatingly than fraud. It gives a handle to those who seek to devalue the role financial institutions play. It undermines the confidence of individual investors - disastrous for an industry whose workings depend crucially on trust.

20 Fraud is a complex crime. It is perpetrated by sophisticated operators. We need sophisticated arrangements to beat the fraudsters. Two years ago we made a start. The Chancellor announced the establishment of fraud investigation



groups - specialist units to co-ordinate the work of the different enforcement agencies.

21 Now we are taking further steps. The Home Secretary has announced changes to rules of evidence and court procedures to make it easier to bring criminals to book. And he announced the creation of a new permanent Government Department - the Serious Fraud Office.

22 I believe the SFO is a vital step forward in the attempt to tackle fraud. Fraudsters do not compartmentalise their crimes - it makes no sense for Government to compartmentalise its response. The FIGs have shown the benefits that can come from a co-ordinated approach. But they have also highlighted the difficulties in ad hocery. The SFO will be a permanent body. It will have its own staff. It will draw on existing expertise. And it will be able to recruit on specialists who can take on fraudsters at their own game. It will work in close harmony with specially selected police officers. There will be a single director of each investigation who will be responsible for investigating and prosecuting in each case.

23 The SFO should have the support of all those who care about the reputation of our financial services industry. It has the Government's full backing.



003/2761

## ECONOMIC SITUATION

We should not make us lose sight of the underlying strength of the economy. The UK is now in its sixth successive year of growth - the longest period of uninterrupted growth since the 1973 oil price rise. And after decades of being left behind our European partners, we have in the past 3 years bettered or equalled their growth rates.

And that growth record has been achieved against a backcloth of falling inflation, now down to 2.4 per cent - its lowest level for nearly 20 years. Inflation is back to the level of the 1950s and 1960s: - and is below the European average.

We're overcoming another problem of the 1970s - low profitability of companies. You do not need me to tell you about the sharp rise in company profits - up by over 20 per cent between 1984 and 1985. The average real rate of return last year reached its highest level since 1964 - three times that of 1975. Partly as a result, industrial investment reached an all time high in 1985.

And manufacturing industry has been sharing in this general prosperity. Manufacturing profitability is at its highest level since 1973. Manufacturing productivity growth here has averaged 5 per cent a year for over five years, second only to Japan. There is no previous five year period in recent history over which manufacturing industry has been so successful in holding its share in world markets.

The results are seen in jobs. Attention always focusses on unemployment. That ignores our success in creating employment. Since June 1983 employment has gone up by nearly



1 million - a better record than the rest of the European Community combined.

But the labour force has been growing even quicker than the number of new jobs. That is why unemployment has continued to rise. But the rapid growth in the labour force does now seem to be slackening, offering us a brighter prospect for the future. Meanwhile we have successfully tackled youth unemployment - the rate of youth unemployment is now lower than in most of the European Community. That is a direct result of the measures we have introduced to help youngsters get the training they need to become an effective part of the workforce. Last week Lord Young announced new initiatives to tackle the problem of long-term unemployment.

I would not deny that economic activity has been more sluggish this year. But, as the Chancellor has said, this pause in growth is temporary. Soon we shall see the beneficial effects of lower oil prices reflected in higher activity here and abroad. There are already signs that our exports are beginning to pick up and domestic demand remains strong. The prospect is for faster growth next year, while the realistic and prudent policies to which we have been committed since 1979 will continue to ensure that we maintain firm control over inflation.

he doesn't use your phrase "lower than the EC average, & falling".



PUP

FROM: N J ILETT  
 DATE: 9 October 1986

CHIEF SECRETARY

Ch.  
 A very few drafting  
 suggestions. Otherwise  
 Seems familiar.  
 HHH

cc: PPS  
 Financial Secretary  
 Economic Secretary  
 Sir P Middleton  
 Mr Cassell  
 Mrs Lomax  
 Mr Scholar  
 Mr Culpin  
 Mr M Hall  
 Mr C W Kelly  
 Miss O'Mara  
 Miss Sinclair  
 Mr Pickford  
 Mr Board  
 Mr Hudson  
 Mr Neilson  
 Mr Cropper  
 Mr Ross Goobey  
 Mr Corlett - IR

CHIEF SECRETARY'S SPEECH TO THE INSTITUTE OF BANKERS, NORWICH,  
 14 OCTOBER

- ... I attach a draft speech, as requested in Miss Rutter's minute of 6 October to Mrs Lomax. The draft is based on contributions from a number of people in FIM and FP.
- ... 2. I also attach the "Sighting Shot" for the initial section on the economy, prepared by Miss O'Mara. This does not of course contain any reference to recent market developments. You had it in mind to issue a local press release on the need for banks and building societies to exercise restraint in the extension of credit. This is covered in paragraph 14 and 15 of the speech. And you want to issue a national release on fraud - paragraph 21-24 of the speech.
3. You may like to see the Economic Secretary's recent comments to the South and East Association of Building Societies on the extension of credit, and the Governor's remarks in Vienna on ... the same ground. I attach these (top copy only).



N J ILETT



**CHIEF SECRETARY'S NORWICH SPEECH****Financial Services**

1. Norwich has a long association with the financial services industry. Members of the Institute of Bankers here tonight will not need me to remind them of the contribution which the banks and other financial institutions are making to the prosperity of East Anglia. At the national level, the output of the financial sector has increased by 50% since 1979.

2. The banking sector is at the forefront of wide ranging and rapid changes.

3. Internationally, the major world markets are becoming one, drawn together by technology and competition. Much of the action is in the UK. The growth of international securities trading, both in equities and eurobonds, is phenomenal. Indeed, the traditional distinction between international banking and international securities has largely disappeared. Big Bang and the associated changes in the Stock Exchange reflect these developments and equip the City for the new world. The Government and the financial services industry have a common objective, to maintain and strengthen the UK's role as a leading world centre of great benefit to the UK economy.

4. I make no apology for dwelling on international



aspects of the changing financial world. Nowhere are these more relevant to the domestic markets or to domestic concerns than in the United Kingdom.

5. Indeed, the forces which are making for change in the international markets have their parallel in the domestic market, in so far as one can distinguish the two.

6. Technological innovation has changed all our lives - not least yours - and is radically affecting the financial market place. Competition is increasing. The distinctions between traditional functions, traditional products and indeed traditional High Street institutions have diminished.

7. From 1 January next year, building societies will be free to compete with the retail banks in many more areas. The banks have, of course, already made their mark in the building societies' traditional market.

8. And the conversion of the Trustee Savings Banks to their new status has strengthened competition in retail banking. It has also made a very substantial contribution to wider share ownership. I welcome the High Street bank with three million owners - truly popular capitalism.

#### **PEPS**

9. I would like to welcome also the contribution



which the banks are making to [the Government's plan to increase share ownership through PEPs - ] Personal Equity Plans. — a further vehicle for extending share ownership which the Chancellor announced in this year's Budget.

10. As many of you will know, PEPs will provide the investor with an attractive means of buying equities up to £2,400 a year. Attractive in two ways. First, the investor will get income tax relief on dividends, provided these are kept within the plan. After a short qualifying period of less than two years, he will get relief from any capital gains tax due if he sells his shares. Second, PEPs is simple, for the investor. The Plan Manager will look after all the documentation and the investor will not need to have any contact with the Inland Revenue.

11. The role of the Plan Manager is clearly vital. So the Government has consulted potential plan managers at all stages in the preparation of the Regulations which will govern PEPs.

12. The banks have played a prominent and most constructive part in that process. Several major banks have already announced that they will offer Personal Equity Plans to the public and I believe that others will follow. [PROBABLY - topical reference to publication of draft Regulations and to Lloyds Bank announcement on PEPs management plans, once we are sure that these events will occur on the day of CST's speech]

13. The banks' customer bases and branch networks



put them in a position to make a very substantial contribution to the success of the scheme and indeed to wider share ownership generally. I am confident that members of the Institute of Bankers will make the most of this opportunity to develop your business and extend your relationship with your customers.

LOCAL PRESS  
RELEASE

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#### Prudential Matters

14. I would like to sound two notes of warning. First, we have seen increased competition in every aspect of deposit taking, lending and financial services. I welcome these developments, and I believe that the financial sector, its customers and the economy generally have benefited from them.

15. Nevertheless, competition brings additional risks. It does not help anybody to go after market share regardless of the likely return on marginal business or indeed of the borrower's capacity to repay. So I hope that banks and building societies will continue to keep a very sharp eye on the quality of the business they do, rather than simply to think about quantity; and that the pressure of competition will not tempt lenders to take decisions against their better judgement or outside their competence.

---

16. Second, your industry can only thrive in a healthy atomsphere. This requires proper investor protection, that is to say effective regulation and the effective detection and prosecution of fraud.



17. The Government has taken steps to ensure that our regulatory framework can cope with the new pressures.

18. The Financial Services Bill, which is now completing its passage through Parliament, will modernise and extend the regulatory framework for investment. The Building Societies Act has updated the regulatory system for building societies. We have announced plans to strengthen banking supervision. And we are developing techniques and systems for the complex task of regulating financial conglomerates which are subject to more than one prudential regime.

19. We have done, and are doing, a great deal. But we cannot afford to rest on our laurels. Financial supervisors have to aim at a moving target. That is as it should be in a world of innovation and competition. It is essential that supervisors should find the right responses to market developments. But it is also essential that supervisors should allow the industry to get on with its job without unnecessary distraction interference or costs. This requires special skills and constant attention. I assure you that the Government is very much aware of the economic cost of regulation.

20. That said, the success of your industry relies above all on your own high professional standards. Your institute is playing a major part in achieving and maintaining these standards. The fact that the supervisors are looking over the industry's shoulders does not in any sense reduce the responsibility of



bankers and other market practitioners to look after other people's money in a responsible and prudent fashion. In this sense the financial services industry is constantly on trial and must remain jealous of its public image.

NATIONAL  
PRESS  
RELEASE

### **Fraud**

21. I turn now to fraud. The Government is determined to strengthen the arrangements for deterring and punishing fraudsters. Two years ago, the Chancellor announced the establishment of the fraud investigation group. This specialist unit in the office of the Director of Public Prosecutions co-ordinates the various roles of the different enforcement agencies which may be involved in particular cases. We have also made more resources available for the investigation and prosecution of fraud.

22. Earlier this month, the Home Secretary announced a wide range of measures to improve fraud investigation and prosecution in response to the Roskill Committee's report. These will include changes to the rules of evidence and court procedures to make it easier to bring cases and to explain to all concerned what fraud cases are about. Also, we intend to establish a new government department, The Serious Fraud Office. I am particularly glad to have had the privilege of leading a study group within the Government which concluded that this new Office is necessary.

23. The Serious Fraud Office will build on the existing work of the Fraud Investigation Group. It will bring



together under a single command investigation and prosecution work on major cases which is currently undertaken by four Government departments; and it will have the assistance of experienced Police Officers specially chosen for the work.

24. This is evidence enough of the Government's determination to maintain the standards of probity which we have a right to expect in this country. Fraudsters are, of course, a tiny minority. But they can do disproportionate damage to the image of our financial services sector, on top of the harm they cause to their victims. We will do everything possible to keep the UK safe for investors.



## EB DRAFT ON ECONOMIC SITUATION

1. The UK is now in its sixth successive year of growth - the longest period of uninterrupted growth since the 1973 oil price rise. In fact we topped the European Community growth league in both 1983 and 1985, and grew at around the average rate for EC countries in 1984 despite a year long coal strike. This is in sharp contrast to the previous decade when we were at the bottom of the league.
2. And we have maintained this excellent growth record against a backcloth of falling inflation, now down to 2.4 per cent - its lowest level for nearly 20 years. Our inflation rate is now below the EC average, back to the levels we saw in the 1950s and 1960s.
3. As bankers, you will not have been slow to notice that company profits in the UK have been rising sharply - up by over 20 per cent between 1984 and 1985. The average real rate of return last year reached its highest level since 1964 - three times that of 1975. Partly as a result, industrial investment reached an all time high in 1985.
4. Despite the stories circulating in the press, manufacturing industry has been sharing in this general prosperity. Manufacturing profitability is at its highest level since 1973. Manufacturing productivity growth here has averaged 5 per cent a year for over five years, second only to Japan. In fact there is no previous five year period in recent history over which manufacturing industry has been so successful in holding its share in world markets.
5. It is industry, not Government, which creates jobs and since we were re-elected in June 1983 employment has risen by nearly one million. The UK has created more jobs than the whole of the rest of the European Community combined. Indeed, another fact which is often not fully appreciated is that we have a higher proportion of the working population in work than most other major countries.
6. However, despite this rapid job creation unemployment has continued rising, although in recent months there has been a welcome improvement in the upward trend. The sad fact is that the labour force has been growing even quicker than the number of new jobs. So that we have to run even faster to avoid slipping back. But the rapid growth in the labour force does now seem to be slackening, offering us a brighter prospect for the future.
7. And even now the picture is not one of unrelieved gloom, for unemployment among the young - a group to whom we have given top priority - has actually been falling and is now



lower than in most of the European Community. <sup>We shall</sup> It is time to tackle the problem of <sup>long</sup> term unemployment and we have devised a package of measures carefully designed to help the <sup>with equal determination</sup> long term unemployed. There is increasing evidence that this will prove successful.

8. What of the future? It is certainly true that economic activity has been more sluggish so far this year, as we have adjusted to the initial impact of the oil price fall. But this has been a general phenomenon throughout the industrialised world. Countries heavily dependent on oil export earnings have of necessity cut back their spending faster than oil consumers have increased theirs. However, I share the Chancellor's view that this pause in growth is a temporary one and that we shall soon see the beneficial effects of lower oil prices reflected in higher activity here and abroad. There are already signs that our exports are beginning to pick up and domestic demand remains strong. So there is every prospect of faster growth next year, while the realistic and prudent policies to which we have been committed since 1979 will continue to ensure that we maintain firm control over inflation.





C.

I understand the CST spoke to you about this at a bilateral. Are you content for him to issue a national press release on fraud, 2 days before the Mansion House Speech?

**RIGHT** I assume he should say nothing whatsoever about market matters.

AH

7 ~~£~~. 10.

yes.





FROM: JILL RUTTER  
DATE: 6 October 1986

MRS LOMAX

cc:  
PS/Chancellor  
PS/Financial Secretary  
PS/Economic Secretary  
Mr Scholar  
Mr Culpin  
Mr Ilett  
Miss Sinclair  
Mr Kelly (C.W.)  
Miss O'Mara  
Mr Board  
Mr Neilson  
Mr Ross Goobey

Mr Corlett - IR

**CHIEF SECRETARY'S SPEAKING PROGRAMME: INSTITUTE OF BANKERS,  
NORWICH, 14 OCTOBER**

The Chief Secretary was grateful for your note of 30 September covering a note by Mr Board. The Chief Secretary would be grateful if you could work up a 10 minute speech covering the points in Mr Board's synopsis A to E, omitting the section on new technology and the section on local "challenges and opportunities." He would like to build up the PEP section.

2 For a national press release he would like to take up your suggestion of doing something on fraud.

3 The Chief Secretary would also like a section, which he could press release locally, on the need for banks and building societies to exercise some restraint in the extension of credit. The Chief Secretary discussed this with the Chancellor who is content for the Chief Secretary to take up that theme in a local release.

4 The Chief Secretary would be grateful for a worked-up text by Thursday evening. He would also like to include an initial piece about the state for the economy. Miss O'Mara, in consultation with Mr Kelly, to whom I am copying this minute, might like to consider what the Chief Secretary might say. I realise that this will need to be updated after the weekend. But again I would be grateful for a sighting shot - not more than 1½ pages - by Thursday evening.

*Jill Rutter*  
JILL RUTTER



FROM: MRS J R LOMAX  
DATE: 30 SEPTEMBER 1986

CHIEF SECRETARY

cc PS/Chancellor ✓  
PS/Financial Secretary  
PS/Economic Secretary  
Mr Scholar  
Mr Culpin  
Mr Ilett  
Miss Sinclair  
Mr Board  
Mr Neilson  
Mr Ross Goobey  
Mr Corlett - IR

**CHIEF SECRETARY'S SPEAKING PROGRAMME: INSTITUTE OF BANKERS, NORWICH,  
14 OCTOBER**

The attached note by Mr Board outlines a number of ideas for your Institute of Bankers' speech in Norwich on 14 October. It would be useful to know whether you are looking for a full draft, or just press release material.

2. You wanted to press release something locally on the role of retail banks in popularising PEPs. In addition to the points in section C of Mr Board's note you will obviously want to congratulate the banks on the imaginative way in which they have responded to the PEPs initiative, and stress their importance in making PEPs a success. The draft PEP regulations will have been published the previous week but it is unlikely that they will contain anything newsworthy. The only point to make is that we have played our part in providing a detailed specification for PEPs: now it is up to the plan managers to go out and sell them. You may want to add some remarks addressed to companies, urging them to give a positive welcome to wider share ownership.

3. You were also thinking of a national press release on a topical banking theme. The possibilities are fairly limited: 14 October is the day after the Financial Secretary's speech on wider share ownership at the Stock Exchange/Daily Mail seminar, and only two days before the Chancellor's Mansion House speech, which will contain a major section on the Big Bang, financial innovation,



and financial re-regulation. I would strongly advise you not to get embroiled in any continuing row over the TSB flotation. Perhaps the most natural topic for you would be fraud: especially the Serious Fraud Office, for which you can reasonably claim credit. But this will be a couple of weeks after the Home Secretary's announcement. If you have not had an earlier opportunity to say something on the SFO it might be more effective to save any reflections from Treasury Ministers for the Mansion House speech. So, unless Mr Culpin has a better idea, I would on balance recommend against a national press release on a financial theme on this occasion.

*Surely financial is trying to cast doubt on the £28 billion!*

*RL*

**RACHEL LOMAX**

*It would be a pity to see any potential power...  
...with...  
...which we spend...  
...at...*



FROM: D R H BOARD  
DATE: 30 September 1986

- MR M HALL  
2. MRS LOMAX  
3. CHIEF SECRETARY

cc PS/Chancellor  
PS/Financial Secretary  
PS/Economic Secretary  
Mr Scholar  
Mr Culpin  
Mr Ilett o/r  
Miss Sinclair  
Mr J Monaghan (CCTA)  
Mr K Murphy  
Mr Neilson  
Mr P Hall  
Mr Ross Goobey  
Mr Corlett - IR

CHIEF SECRETARY'S SPEAKING PROGRAMME: INSTITUTE OF BANKERS, NORWICH,  
14 OCTOBER

Miss Rutter's minute of 13 August reports your thoughts on possibilities for this speech. FIM 1 and 2 have considered this jointly. At local level you might, we suggest, refer not only to the role of retail banks in popularising PEPs but also to Norwich/East Anglia facing the challenge of successfully operating in the new financial services revolution. Further local colour plus a link with new technology would also flow from some reference to CCTA in Norwich. Shifting to a wider plane, you could reasonably point to the establishment of the Serious Fraud Office and your personal involvement in that. Depending on the Labour Party conference Mr Ross Goobey might want to insert some comment on the Labour Party's attitudes and policies towards financial services.

2. These points are set in context in the attached skeleton outline. If you are content with it and with our suggested highlights, we will work up (with CCTA) some speaking notes and draft passages for press release.

Seems fine to me.

~~###~~

*Douglas Board*  
D R H BOARD



## CHIEF SECRETARY'S SPEECH: INSTITUTE OF BANKERS, NORWICH, 14 OCTOBER

Draft outline

## A. The exploding financial universe

- pace of innovation, driven by international competition and technological change
- financial services fast[est?] growing sector of economy
- Big Bang only one aspect
- other aspects include global 24 hour markets, securitisation, narrowing margins.

## B. Position of Norwich

- long association with financial services industry [regional statistics?]
- must face up to challenges and opportunities, eg improving local access to central markets

## C. Challenges and opportunities for retail bankers

- High Street competition intensifying
- 1 January 1987: "Big Bang" for building societies, competing in new areas.
- TSB flotation both a stimulus to competition and a boost to wider share ownership
- Banks looking for new areas of business to develop, wider share ownership a good chance to use banks' retail networks



- Shareships
- PEPs (comments on recent announcements by, eg, NatWest - attached) *Draft PEP regulations would just have been published (week beginning 6 October)*

#### D. Challenges for regulators

- need for appropriate responses from regulators to financial services revolution (new instruments, off-balance sheet risks);
- need for co-ordination between regulators nationally (lead regulator concept) and internationally;
- ultimately weight of regulation/intervention of statute dependent inversely on degree of professionals' (eg bankers') self-discipline and high standards (eg Banking Ombudsman).

#### E. Challenges for criminal authorities, judicial system

- new opportunities in rapidly-changing financial world include new opportunities for crime;
- the authorities' response to fraud. Roskill. Serious Fraud Office
- prevention better than cure, bankers must play their part

#### F. New technology

- new technology a powerful driving force in financial services revolution
- that is only one example of impact of new technology
- Treasury directly concerned with new technology through CCTA, represented in Norwich (examples).



Page 7

Reference Financial Times

Friday 26.9.86.

## NatWest to offer Peps

NATIONAL WESTMINSTER Bank will be offering three personal equity plan (Pep) schemes from January 1 1987.

Under the first scheme, individuals will pay a regular sum of between £20 and £35 (the maximum set by the Government for unit trust investments to qualify for tax relief), a month, which will be invested in one of the unit trusts run by County Bank.

Under the second scheme,

they will pay a regular sum of between £36 and £200 (the maximum set by the Government for direct equity investments to qualify for tax relief) a month, which County Investment Management will then invest on their behalf.

Only under the third scheme will people be able to manage their own investments. They will pay a yearly amount of between £1,200 and £2,400.



~~MA~~ CST

OXFORD FARMING  
CONFERENCE



CONFIDENTIAL

PHF



FROM: A P HUDSON  
DATE: 20 OCTOBER 1986

PS/CHIEF SECRETARY

cc Sir P Middleton  
Mr F E R Butler  
Mr Monck  
Mr Lavelle  
Mr Burgner  
Mr Edwards  
Mr Scholar  
Mr Bonney  
Mr Culpin  
Mr G M White  
Mrs Imber  
Mr Tyrie

**OXFORD FARMING CONFERENCE 1987**

The Chancellor has seen the outline speech attached to Mr Bonney's 9 October minute.

2. He has commented that there are two key points to get across loud and clear, both highlighted in his Development Committee speech in Washington (final text circulated with my minute of today):

- a. The sheer nonsense of the present system worldwide;
- b. The need for a market solution.

AHH

A P HUDSON



CHIEF SECRETARY

FROM  
DATER J BONNEY  
9 OCTOBER 1986

cc

PPS ✓  
 PS/Sir P Middleton  
 Mr F E R Butler  
 Mr Monck  
 Mr Lavelle  
 Mr Burgner  
 Mr Edwards  
 Mr Scholar  
 Mr Culpin  
 Mr G M White  
 Mrs Imber  
 Mr Tyrie

**OXFORD FARMING CONFERENCE 1987**

Mr Pegler's minute of 18 July asked us to submit a synopsis of your paper for this conference during September. I am afraid that pressure of other more immediate work has delayed this a little. I now attach a draft synopsis prepared by Mrs Imber for your consideration.

2. The theme for the conference is "Realism in Agriculture" and you have been particularly asked to cover the Government commitment and ability to pay for a prosperous countryside/farming in the UK. Mr Pegler's minute suggested that you would wish to include a comparison between the cost of supporting farmers with the Government's support for industry. We would see this paper as a useful opportunity to get into the public domain some of the calculations prepared for the Prime Minister in 1984 (on a "secret and personal" basis) but would need to seek MAFF's help to update the figures which are now getting a bit dated. Are you content for us to approach MAFF on this point? The alternative would be to rely solely on the public expenditure comparison derived from the Public Expenditure White Paper but this would exclude the very considerable economic costs of CAP protection.

3. You will wish to consider to what extent you wish to comment on the prospects for individual commodity regimes. The present draft suggests short passages on three of the main sectors of interest to the UK - dairy, cereals and beef. Alternatively



you might prefer to stick to the principles which should influence our approach to all of the commodity regimes: e.g. reducing prices to nearer market clearing levels; returning intervention to its original safety net role not as a standard marketing outlet; introducing more flexibility into the operation of CAP regimes to remove the incentive to unlimited production at guaranteed prices.

4. Finally, you will wish to say something about the Government's policy towards structural changes and diversification. This may be easier to draft following the Prime Minister's meeting on 6 November to discuss Mr Jopling's alternative land use proposals. We would hope that it will be possible to take the line that there is no automatic presumption that the Government should intervene to forestall structural changes in the agricultural sector. But that there may well be a case for redirecting some of the resources currently [mis]directed in encouraging [and subsequently dealing with] surplus production in ways which would encourage diversification of the sources of income and employment in the countryside.

5. You may wish to discuss before we submit a full version of the draft.



R J BONNEY

Chr.

Outline attached does not always bring out points clearly, e.g. para 13 buries the critical point about the need for a market solution in amongst more specific detailed points.

2 key things emerge from your Development Ctee speech:

(a) the sheer nonsense of the pres. system worldwide;

(b) the need for a market solution.

004 1151

X | I suggest we simply advise CST that these are the things to get across loud & clear. AH



OXFORD FARMING CONFERENCE 1987

TUESDAY 6 JANUARY 1987

PAPER BY THE CHIEF SECRETARY TO THE TREASURY

SYNOPSIS

A Worldwide problem

1. Agricultural support a world wide problem. Combination of protectionism in the industrialised countries and discrimination against agriculture in the less developed countries depressing global economic output [examples], Liberalisation estimated to yield \$41 billion in efficiency gains ( ref World Bank Report) Quotation from the Chancellor's Development Committee Speech.

2. Where do we fit in? Inextricably bound up with the CAP. But not entirely so - some purely domestic support eg structural assistance and R&D. Objectives of the CAP. Three main aspects to support - intervention, subsidised exports and tariff barriers against imports. [ examples of extreme cases] All serve to reduce risk and to move agriculture further from the disciplines of the market. Need for reform to move closer to free market with a safety net for stability of supply for the consumer and income for the producer.

Surpluses

3. Support through price fixing, backed by intervention and production subsidies eg to oil seed crushers. Support prices set too high in relation to market demand. Result growing surpluses. Over three times as much beef - 670 thousand tonnes - as in 1981 Rapidly reaching the point where butter stocks ten times the 1981 level (185 thousand tonnes) No sign of abatement . Cereals intervention stocks 17.5 million tonnes - on current trends 80 million tonnes by 1990.



Funding

4. These mountains are initially funded by the Member State. In 1985-86, the UK taxpayer directly spent £xxx on intervention stocks y % more than ten years ago. The EC pays for any loss on disposal and pays for part of the costs of storage and finance charges. Across the EC as a whole over £2 billion spent on simply maintaining the stocks.

Costs of Disposal

5. Stocks would be even higher without special disposal measures. On the internal market special disposal schemes range from butter for pensioners to sales for animal feed. Irony the latter are more financially effective. System of export refunds to boost exports by bridging the gap between high internal support price and low world price. Examples butter and grain to the Soviet Union, beef for processing to Brazil. Export refunds are one third of the CAP budget. Most of world's food exports now grown by industrialised countries where costs of production are high and consumed in developing ones where costs generally lower. Agricultural surpluses depress world prices. Industrialised countries competing in the dumping of surplus commodities on the world market.

Tariff Barriers

6. To complete the circle of protectionism we keep out potentially cheaper imports by tariff barriers. Some £1 b of the EC Budget is financed through agricultural levies, £175 m collected at UK ports.

Other support

7. Support for special areas. Capital grants (£130m) HLCAs (£110m) government funding of advisory services and research - £x m compared with £ m for manufacturing industry. Tax concessions in addition to those afforded to manufacturing - rates, fuel duty, VED



Benefits

8. What do we gain? Security of supply. Self sufficiency measures/comparisons. Preservation of rural economy/ecology. Maintenance of farm incomes? Despite support. Farm incomes have fallen in real terms since the 1970s

Costs

9. How much does all this cost? In 1986 cost to the EC budget over £15 billion, of which the UK taxpayer contributes £3b. £1.3 b spent in UK. In addition UK Exchequer pays out an additional £1.4 billion [£0.5b net cost of the CAP £0.9 b on domestic support] Difficulties of forecasting/estimating controlling costs. Historical overspends But the economic cost is far greater. Price support, assistance with exports and other direct support are worth over £3.6 billion a year - equivalent to 70% of the value added to GDP. Taking account protection against imports adds another £2 billion, raising the economic bill to over 100 % of the net contribution to GDP. Manufacturing industry receives far less.

10. Unless something done, costs keep on escalating. Costs of storage rising by X each year By 1990s it would cost Y to simply store surpluses, Z to dispose of them, if markets could be found. Unless a solution can be found CAP collapse under its own weight. Least disruption through planned action

EC Budgetary Constraints

11. Growth in CAP expenditure. 23 b ecu in 1986 compared with 12 b ecu in 1979. Reduced reimbursement for Member States. Financial Guideline. Effect of dollar on world prices. Increase costs of disposal. Already know Budget in difficulties for 1987.



Solution

12. What can be done? Growing support for reform in international fora. Tokyo declaration. OECD research. GATT negotiations.

13. Three principles - strong measures to reduce surpluses backed by some structural support, equity of treatment between Member States, consumers and producers, room for enterprise. All this means moving closer to the market, above all a sensible price policy to bring the market back to equilibrium. In the long term interest of the efficient, British, farmer. More effort into the marketing less into sheer production. Not easy resistance by other Member States.

Specific Sectors

14. Three main sectors - dairy, cereals, and beef. Relative shares of expenditure UK and EC. Prime aim reduce surplus production and wasteful expenditure on stocks.

15. **Dairy** Painful steps taken by Council two years ago with the introduction of quotas and the super levy, but that has proved too little too late and the superlevy had to be introduced last year. Yet still production rises. Latest sign some deceleration in rate of increase. Commission emergency measures. Discussions with New Zealand and other exporting countries for orderly management of market.

16. **Cereals** First step taken at the last price fixing, restrictive measures [list], including introduction of co-responsibility levy. Need to avoid crisis management of milk sector. Quotas a second best solution. Restrictions on use of nitrogen. Important not to cut efficiency when cutting production. Land diversion. Alternative crops. Role for individual enterprise.



17. **Beef** Problems of beef intervention. Intervention not a good way to help producer or consumer. Costs of freezing - both deterioration of quality, limited life, marketing difficulties. Interaction with milk sector. Role of premia. Consumer and farmer benefit. Reform priority of UK Presidency of EC. Commission proposal. UK objective reduce costs but retain adequate support to producers.

Summary

18. International recognition that something must be done to combat mounting stocks and world wide marketing difficulties demonstrate the need for reform. Importance of working together towards a market solution rather than tight government control.



CST

SUN LIFE

INVESTMENT  
SEMINAR

~~1988~~



PlwP

1. Computer, pl.  
2. Back to me pl.  
AMH



FROM: M C FELSTEAD  
DATE: 21 October 1986

MR ROSS GOOBEY

- CC:
- PS/Chancellor
- PS/Financial Secretary
- PS/Economic Secretary
- PS/Minister of State
- Mr Monck
- Mrs Lomax
- Mr Peretz
- Mr Turnbull
- Mr Culpin
- Mr Gilhooly
- Miss O'Mara
- Mr Cropper
- Mr Tyrie

**SUN LIFE INVESTMENT SEMINAR: 1 DECEMBER  
THE GOVERNMENT'S ECONOMIC STRATEGY**

As discussed, the Chief Secretary would be grateful if you could have a go at a first draft of a speech for this seminar. I will be arranging a short meeting for you to discuss the main themes with the Chief Secretary.

... 2 I attach a copy of the Chancellor's speech given to the Sun Life Investment Seminar last year, to give you an idea of what the audience might be expecting. I think the speech was drafted by Mr Howard Davies - the Chancellor's Special Adviser at that time. The speech looks to be around 20 to 25 minutes in length.

M C FELSTEAD  
Assistant Private Secretary





*for ...  
-asked ... make speech  
MLF  
11.10.85*

# H. M. TREASURY

Parliament Street, London SW1P 3AG, Press Office: 01-233 3415  
Telex: 262405

30 October 1985

## CHANCELLOR'S SPEECH TO SUN LIFE INVESTMENT SEMINAR

Attached is the text of the Chancellor's speech to the Sun Life Investment seminar, held at the Cafe Royal, London, today.

PRESS OFFICE  
H M TREASURY  
PARLIAMENT STREET  
LONDON SW1P 3AG  
01 233 3415

148/85



SUN LIFE SEMINAR: 30 OCTOBER

It has been an interesting fortnight. Two weeks ago, I made my Mansion House speech.

Among other things, I indicated that inflation would probably be below 4 per cent by the middle of next year, and that the economy would continue to grow at a healthy rate for the sixth successive year.

I reaffirmed that we have every intention of keeping in place the policies that are bringing this about - policies of sound money and free enterprise.

Since then I have been attacked from two sides.

Some in the City concentrate on a particular measure of the money supply.

They believe it is growing too fast.

They accept that inflation will come down for the immediate future, but they see bad times just around the corner.

A surge in inflation as the liquidity being built up spills over into spending.

Others, in industry, concentrate on interest rates and the exchange rate.

They find both uncomfortably high.

Their worry is not that there will be an inflationary boom but that, in our determination to defeat inflation, we risk applying too much of a brake to the economy, and choking off economic growth.

It is by no means unusual to find these criticisms on different pages of the same newspaper.



On one page, I am told that our policies are too expansionary - stoking up inflation for the future.

On another page, too contractionary - threatening to crucify British industry.

It is tempting to say that if I am being attacked from both sides, then we are probably getting the balance about right.

And there's clearly something in that.

But it may be more interesting to look behind the headlines to see what our critics really expect to happen.

Take inflation first.

No one now doubts that we are over the "blip" - the temporary increase that I forecast in the Budget.

No one now doubts that inflation will fall in the rest of this year and on into next.

Then take growth.

No one is arguing that it is about to grind to a halt.

We have had the longest upswing since the War, and everyone expects it to continue.

What is at issue is whether growth next year will be, say, 2 per cent or  $2\frac{1}{2}$  per cent or maybe 3 per cent.

That it will be positive and significant is not in doubt.

So if you look at what people in the City and in industry actually expect, it is not very different from what we in the Government expect.

Lower inflation and sustained growth.



Not an unacceptable combination.

And we all reach similar conclusions because we look at similar evidence.

Again, take inflation first.

The latest CBI survey, reported in today's papers, shows that the number of firms expecting to raise their prices is the lowest for seventeen years.

Despite the excessive growth in earnings - of which I shall have more to say later - the number of firms expecting their costs to rise is the lowest for 22 years.

A prospect which, of course, owes much to a firm exchange rate, and low commodity prices.

Or take growth.

I see no sign at all that the economy is running into the traditional buffers.

In the past, economic upswings have invariably been accompanied and indeed boosted by companies building up their stocks.

They have then tailed off when companies started to run stocks down again.

But the latest recovery owed little to stockbuilding.

Many companies have managed to economise on stocks while increasing their output.

Stock/output ratios are by no means high; so the chances that growth will be checked by a sharp rundown in stocks are much less than in earlier periods.



Nor do I see a major downturn in investment.

We knew, of course, that there would be a surge in investment as a result of the tax changes I introduced in the 1984 Budget.

The surge was, if anything, larger than we expected.

Over the last year, both business investment and manufacturing investment have grown by nearly 14 per cent, in real terms.

Many said there would then be a dip.

Investment would fall after the initial surge.

True, it is not going to rise as fast next year as it has this year.

No one would expect that.

But I see no sign of a fall.

Indeed, I expect business investment to grow as fast as the economy as a whole.

The CBI has predicted a further strong growth in manufacturing investment well into 1986.

That is driven in large part by better profits.

Manufacturing profitability is at its highest since 1973.

And the CBI's own survey this week showed that the prospect for orders and employment is about the same as a year ago.

Business optimism, too, is roughly at last year's level.

Over the past year we have had the fastest growth for over a decade - higher, in all probability, than any other major European country, or even the US.

As well as increasing the number of people in work, there are now welcome signs that this is beginning to affect the level of



unemployment.

Our policies are delivering lower inflation and steady growth.

You all know what these policies are.

They have been the same, in substance, since 1979.

Financial discipline to defeat inflation.

Free enterprise to generate growth and jobs.

Contrast the prospect we now face with the gloom of four or five years ago.

Then the question was: "where will the growth come from?"

Some even sought to prove it couldn't come at all.

No one even asks that now.

The questions are simply how strong the growth rate will be, and how much inflation will come down.

This combination of steady growth at 3 per cent a year with no resurgence of inflation has been unknown for a generation.

But what of the longer term?

There the prospects for growth and employment depend pre-eminently on the way our markets work - the way people respond to the challenges and opportunities of the market place.

Of course the economy will in time have to adjust to a lower level of oil production.

But it will be a gradual process.

We are not yet even half way through our period of self-sufficiency



in oil.

And the decline of North Sea production will be very much slower than the build-up.

The key to successful adjustment will be a flexible and responsive economy.

Inflexible economies react slowly and painfully to change; that's been at the heart of our problems in the past.

And it's a major reason why unemployment rose so sharply and remained high for so long.

The only long term answer is to give priority to strengthening our markets and making them work better.

As we have.

First, by getting businesses out of the public into the private sector - by privatising them.

The privatisation programme has been an outstanding success.

A fifth of the state sector of industry has already been privatised.

I expect another fifth to go by the end of this Parliament.

This is no flash in the pan.

The privatisation programme is only now getting into top gear and will continue for many years to come.

We have sold 51 per cent of British Telecom; but there is 49 per cent still to go.



Telecom has paved the way for gas.

Gas will pave the way for water, and so on.

Each time the frontiers are pushed back, further possibilities emerge.

Second, there have been the changes in trades union legislation.

These have brought about a dramatic change in the way in which unions operate, and particularly in the relationships between union members and their leaders.

Throughout the country, and throughout the trade union movement, the measures to increase the accountability of trades unions to their members have had an enormous impact.

Take the NUR dispute with British Rail over guard manning - a vivid illustration of the way in which power within unions is shifting back to the individual members.

And a number of unions, like the EETPU, have made no-disruption agreements with employers.

They have agreed to new methods of negotiation whose aim is to avoid the old strike based confrontation.

The very recent formation of the Union of Democratic Mineworkers is only the most dramatic illustration of the changing climate.

We always knew it would take time for the full effects to be felt. But we can now look forward to enjoying the benefits of a new



realism amongst those who bargain for their members' pay and jobs.

Third, this will be buttressed by all that we are doing to get a better trained workforce, with skills attuned to the future, to encourage the growth of small businesses and the self-employed, and to get rid of unnecessary rules and other burdens on business.

Of course there are difficulties and uncertainties.

One is the international prospect.

The US is running a massive trade deficit while Japan has a correspondingly large surplus.

As a result, we have seen the emergence of dangerous protectionist pressures in the United States.

It is vital that we resist them, and I and my fellow Finance Ministers are resolved to do that.

Another set of problems is closer to home.

British industry - both sides - still have to come to terms with the implications of a serious medium term commitment to low inflation. Many companies are still giving their workforces pay rises which result in our unit labour costs rising faster than our competitors'.

They went up nearly 5 per cent last year in manufacturing, compared with only 2 per cent in the United States.

In Japan and West Germany they fell.

I know that some would like us to relieve the competitive pressures on industry, brought about by excessive pay settlements, by



engineering a lower exchange rate for Sterling.

This would make it easier for companies to put up their prices.

But it would also add to costs.

To listen to industry's complaints about the exchange rate, you would never think that today's rate is little different from its average over the past 2½ years; and since the G5 agreement last month, we have had a somewhat lower rate against the DM to balance a higher rate against the Dollar.

I know, too, that others would like the Government to relieve the cost pressures on industry by reducing National Insurance contributions.

But the social security system has to be paid for - and employers contribute less in this country than overseas.

If employers' contributions are reduced, then unless benefits are cut correspondingly, someone has to make up the difference.

I do not hear many suggestions as to who this should be.

I know, finally, that some would like us to reduce cost pressures by reducing interest rates.

I well understand this concern.

But interest rates have come down 2½ per cent since the peak.

And the worst thing we could do for British industry would be to put at risk our continuing progress on inflation.

The blunt truth is that, if companies agree excessive pay settlements, they cannot expect the rest of the nation to come to their rescue - whether by subsidising those pay increases, at the



expense of the taxpayer or by taking risks with inflation.

The sad fact is that the price of such behaviour is paid not just by the companies concerned, but also by those they might have employed.

These are the real problems we should all be addressing - if we wish to combine the continued low inflation and healthy growth that is clearly in prospect with a sustained fall in unemployment.



FST's

Chelmsford

Women



PWP



**FROM: J J HEYWOOD**  
**DATE: 28 October 1986**

**MR ROSS GOOBEY**

cc **PS/Chancellor**  
Mr Culpin  
Ms O'Mara  
Mr Hudson  
Mr Cropper  
Mr Tyrie

**FST's SPEECH TO CHELMSFORD WOMEN**

The Financial Secretary was most grateful for your draft.

2. I attach a slightly revised version on which you and copy recipients may have further thoughts and suggestions.

**JEREMY HEYWOOD**  
**Private Secretary**

ENC



FST SPEECH TO CHELMSFORD WOMEN

1. As we move into the last eighteen months of this Government it is time to take stock: where we have come from where we are now and where we are headed in the future.
2. Before the Party Conference season there was a feeling abroad that perhaps the Party had run out of ideas, and was even becoming divided on the solutions being sought for our remaining problems. Indeed, having achieved what we have achieved, the electorate thought it might be safe to go back into the water where some years ago they had fled from the sharks.
3. All that has been dispelled by the successive conferences.
4. The SDP conference in Harrogate was interesting if a little other-worldly. If I was marking it in an ice-skating championship they might get 3 out of 6 for content but only 1 out of 6 for style. The sight of legions of ex-Labour Party members thinking out loud is never going to rival Postman Pat for entertainment value.
5. But the content, although deeply felt, was like a Fabian Society debate and did not relate to the world you or I inhabit. On taxation, on wages policy, on defence, we had policies which were so complicated that even the boffins who had invented them were unsure what their effects would be.
6. How many taxpayers would be paying more under the redistribution scheme, and from what level?



Mr Taverne's answers were not acceptable to Dr Owen so it was back to the drawing board. Dr Owen said that unfortunately he'd been on holiday at the time it had been drawn up.

7. The scheme to tax "inflationary" wage settlements is similarly flawed. It is hideously complex and cannot of course be applied to public employees, where often the problem has arisen.

8. Finally we had defence and the Euro-bomb. No matter that the idea was technically a non-starter and would almost certainly be more expensive than Trident, at least the SDP did come up with a defence policy.

9. But then we moved to Eastbourne and the Liberal conference. Not many marks here for content or style. You here in Chelmsford have had plenty of experience of Liberal pavement politics, and need no guidance from me about how it develops. The grass-roots Liberal concern for cracked pavements has built them up a base of support in local elections. But ad-hoc policy-making to meet local problems does not translate to national politics.

10. Liberals have now had three defence policies in three months. The Euro-bomb, a non-nuclear policy and now a policy which hangs on to Polaris until it can be negotiated away. What happens if, after their successful negotiation has failed to occur before Polaris is obsolete? You may well ask.

11. Ah, say the Liberals, we're not going to tell you what we will replace it with. Not because it's a secret, but because they don't know, and if they said it would split the Party again.



12. The Parliamentary Liberal Party must be unique in the world: it is against the peaceful use of nuclear power in electricity generation, but it is in favour of the use of nuclear power as a military deterrent.

13. If we were not discussing the safety of our nation, it might be amusing. But these are the people who are trying to win this seat and aim for the balance of power in the nation as a whole. The only Alliance that exists in Britain today is between the Liberals and the Labour Party. They did it in 1976 and they'll do it again.

14. After Eastbourne, our attention moved on to the Labour conference in Blackpool. Well, I think it was the Labour conference but with the emollient image, it might have appeared at first sight to be a rose grower's convention. Good marks for artistic impression perhaps.

15. Even the words have been changed to try to fool the electorate. No longer is it Nationalisation but Social Ownership; no longer do we have Exchange Controls threatened, but fiscal incentives; no longer pacifism but talk of dying for one's country.

16. Do they really believe we are as soft as that? The vocabulary has changed but the policies haven't. They are fundamentally the same ones that were offered twenty years ago; but in the case of defence, even more extreme. They failed before and they would fail again. Planning is no substitute for enterprise. Central control is no substitute for personal choice. Nationalisation is no substitute for de-regulation and competition. Unilateralism is no substitute for a Western alliance which has kept the peace in Europe for 40 years.



17. Our own conference in Bournemouth was a marked contrast to these sideshows. We presented a united and experienced team of Ministers with achievements to be proud of and policies for the future.

18. Can it really be only 8 years since the Winter of Discontent? Only 10 years since Denis Healey came back from the airport to do the bidding of the IMF and slash public expenditure? It seems an age ago, so much has happened since.

19. And this is a danger. There will be voters at the next election who cannot remember 27% inflation, strikers picketing hospitals and crematoria and the word ungovernable being used about our nation. We must remind them.

20. This Government has reduced inflation to the lowest it has been for 20 years. Employment has been growing continuously for over 3 years; the longest period of continuous employment growth for <sup>almost</sup> 30 years. The basic rate of income tax is at its lowest for over 40 years and the number of strikes the lowest for almost 50 years.

21. These are hard-won achievements, and seemed unattainable in the 1970s. And because we have won these battles does not allow us to relax. Inflation is never beaten, and if attention lapsed it would be back to confiscating the savings of the old, and making life impossible for the poor. Labour have said that they will undo all the progress we have made on trade union reform. Who knows what would happen if they were ever given the chance. Only the Conservatives want to cut taxes further, every other party wants to increase taxes.



22. There remains much to do. I know the concern on the doorstep is concentrated on three areas: unemployment, the health service and education.

23. The September unemployment figures showed the sharpest fall since we came to power in 1979. The combination of growth picking up in the economy and the employment measures we have introduced are at last beginning to demonstrate their effect.

24. I know that, despite the fact that we have increased spending on the health service enormously since 1979, over and above inflation, public perception is that the health service has suffered cuts. Norman Fowler has undertaken to reduce the hospital waiting lists which cause greatest distress, and the provision of new hospitals continues apace. Technology in healthcare is advancing at such a rapid pace that treatments which were impossible only ten years ago are now commonplace. Demand for healthcare is limitless and it will always be a struggle to keep up with it. It is no good promising the moon as Opposition Parties do. Labour when in office were responsible for the most damaging cuts the NHS has ever suffered.

25. On education too we have been able to suggest new ideas. Kenneth Baker has announced City Technology Colleges which will prepare children from some of our most underprivileged areas for the work of the future. We hope that teachers will see that further disruption will not achieve the aims of any of us: good teaching should receive fair reward and good teaching will train our children for work. Essex under the Liberals has introduced "peace studies", Brent under Labour has plans for racial awareness officers and Haringey for positive attitudes to homosexuals. Even if you believe these



things are desirable, they should not and must not take priority and funds from the basic tasks of teaching: literacy, numeracy and job skills.

26. Perhaps most of all the Conservative conference put paid to all the talk of wets and dries. We all have a similar vision of the society we wish to build and we all agree that the policies of the Sixties will not provide the solutions to the problems of the Eighties and Nineties.

27. If we can concentrate on continuing to return power to the individual, through home and share ownership, through privatisation and de-regulation, through choice and personal responsibility, the gains of the past seven years will be consolidated and made irreversible. We have seen and suffered under socialism, we have seen where the SDP came from and whom the Liberals supported. We alone offer the electorate a positive solution leaving the three Opposition Parties to fight for the minority collectivist vote between them.

28. The Government has no intention of letting the nation slip back again, and, with your help, we will mobilise the country to make this certain.



CST

FOOD + DRINK  
MANUFACTURERS ASSOC.

28/10/86





RWP

FROM: A P HUDSON  
DATE: 28 OCTOBER 1986

PS/CHIEF SECRETARY

cc Mr Culpin  
Miss O'Mara  
Miss Sinclair  
Mr C W Kelly  
Mr Richardson  
Mr Tyrie

**CHIEF SECRETARY'S SPEECH TO FOOD AND DRINK INDUSTRY**

The Chancellor has seen the draft paragraphs on interest rates attached to Mr Richardson's 27 October minute.

2. The Chancellor has commented that it is essential that paragraph 2 should be amended, so that the second and third sentences are deleted ("This will save ... wage rises"), and the words "for a whole year" inserted at the end of the original fourth sentence. It has been consistent policy not to make the point as drafted, first because it implies that interest rates are fixed for a year at a time, which they are not, and second because it is used against us whenever interest rates go up.

A handwritten signature in black ink, consisting of the letters 'A P' followed by a stylized flourish.

A P HUDSON



FROM: M G RICHARDSON

DATE: 27 October 1986

- 1. MR KELLY
- 2. MS RUTTER

cc: Chancellor  
 Mr Culpin  
 Ms O'Mara  
 Ms Sinclair  
 Mr Tyrie

CST SPEECH TO FOOD AND DRINK INDUSTRY

You asked this afternoon for a couple of paragraphs on interest rates for the CST's speech. I attach a draft passage. This does not give much emphasis to the Government's inflation achievements (lowest levels since the 1960's etc), on the assumption that these are mentioned elsewhere in the speech; if an extra puff is wanted, the end of the first paragraph could be beefed up accordingly.

C.

*M G Richardson*

M G RICHARDSON

- 1. CST is speaking tomorrow (Tues).
- 2. Full draft below, but I ~~don't~~ think the only thing you will want to consider is the line on interest rates - see my concern below.

*Attention - rates ANH*  
~~go up. (a) Mr...~~  
~~because as go...~~  
~~that's not the same...~~

*1. I have presented. 2. This has been our...*  
 (a) because...  
 (b) because it is used...  
 (c) because it is used...  
 (d) because it is used...



DRAFT

... Which brings me to interest rates. I fully realise that the rise in base rates a couple of weeks ago was unwelcome to many here today. The Government has no wish to see interest rates any higher than is necessary. Equally, however, we have no intention of abandoning the prudent and responsible monetary and fiscal policies that have underpinned the management of the country's economy since 1979. The Government remains determined to maintain monetary conditions that place steady downward pressure on inflation. Interest rates are the essential instrument of monetary policy, and will be held at whatever levels are consistent with our inflation objectives. To this end we have repeatedly shown ourselves ready to act decisively when this is necessary. Not to do so would be to jeopardise the very real benefits of our inflation achievements to date.

*I might point out that*  
 2. <sup>h</sup> Base rates are still 1½ per cent lower than before Nigel Lawson's last Budget, despite the recent increase.

~~This will save industry more than a quarter of a billion pounds this year. The main problem for industry is not interest rates but wage rises.~~

*I might point out, also, that*  
 One per cent on wages costs industry over £1 billion a year - *for a whole year.* four times the cost of one per cent on interest rates. Indeed, if UK industry succeeded in holding down its labour costs, there would be more scope for reducing interest rates without taking risks with inflation.

C.

I don't like this formulation much. The first sentence suggests that interest rate cuts are some sort of Govt handout. And the second sentence is a pretty sweeping generalisation which some industrialists would no doubt question. Hence ~~is~~ the suggested redraft.

||||



Andrew

PWP

FROM: MISS M O'MARA  
DATE: 23 OCTOBER 1986

CHIEF SECRETARY

cc PS/Chancellor  
Mr Culpin  
Mr S J Davies  
Mr C W Kelly  
Mr Pickering  
Mr Tyrie  
GC/01

12/2

**SPEECH TO FOOD AND DRINK MANUFACTURERS' ASSOCIATION: 28 OCTOBER**

I attach a short draft speech along the lines requested on Wednesday.

2. You are particularly anxious to discuss the level of interest rates. Given market sensitivities, I have tried to cover this in a fairly timeless way and to lead straight back to the problem of pay along familiar lines. But I should be grateful if Mr Kelly would confirm that this will cause no problems.

MOM

MISS M O'MARA



There are those who accuse this Government in general, and the Treasury in particular, of little concern for the fate of industry as a whole and no concern for the manufacturing sector. Nothing could be further from the truth - and I speak as a former Industry Minister. For we all recognise that it is industry, not Government, which creates jobs; and industry, not Government, which creates the wealth on which those jobs depend.

What industry needs most of all is a stable economic framework within which enterprise can thrive and business prosper. We have provided just that. From the moment we came into office in 1979, we have given pride of place in our economic strategy to the defeat of inflation. For the control of inflation is the essential basis of a steadily growing economy.

In May 1979, inflation was running at 10 per cent and rising. Today it is only 3 per cent and we are aiming to bring it right down to zero in the next Parliament. Our success on this front has in turn laid the foundation for healthy growth in the economy, with national output rising annually at nearly 3 per cent over the last 5 years - the longest period of sustained economic growth since the oil price hike of 1973.

Industry has blossomed in this supportive environment. Last year, companies over all earned an average rate of return of 12 per cent - higher than in any year since 1964 and three times the level in 1975. Industrial investment outside the oil sector rose over 8 per cent last year to reach an all time high and rose still further in the first half of this year.

Despite the gloom and doom reflected in some sections of the press, manufacturing has shared in this success. Manufacturing productivity has risen by a remarkable 5 per cent a year on average over the last five years. Manufacturing output is over 12 per cent up since



its trough at the beginning of 1981 and exports of manufactures now stand at an all time high. Indeed, the performance of our manufacturing sector in holding its market share and keeping pace with world output over the last five years cannot be matched in any comparable period in recent history. Small wonder that manufacturing profitability reached 7 per cent last year - its highest rate since 1973 - and that manufacturing investment has risen over 30 per cent since the last election.

Much ink has been spilled over the slowdown in growth the UK economy has experienced since the beginning of this year. There are those who claim that we have entered the downswing of the cycle and others who are concerned we shall generate insufficient demand for the goods British industry produces. I believe these fears are misplaced.

The pause in activity we have seen over the last few months is a temporary one, induced by the economy's immediate response to the collapse in the oil price. It is not surprising that the world's major oil exporters should cut back their demand for manufactured goods from overseas as soon as their oil earnings began to fall - and those are markets in which British industry has a particularly strong presence. By the same token, the world's major oil importers found themselves better off as their purchases of oil became cheaper. But it has taken them rather longer to adjust their spending patterns and increase their imports of other goods. So the growth of world trade as a whole has slowed and, like the rest of the industrialised world, industrial production in the UK remained pretty flat over the first half of this year.

But we are now starting to see some more encouraging signs that growth is beginning to pick up again. Manufacturing output rose over  $\frac{1}{2}$  per cent in the latest 3 months and last week's trade figures showed that our manufactured exports have renewed their strong upward trend. Output is beginning to rise overseas too, as the latest figures from Germany and France reveal. This bodes well for world trade prospects next year.



At the same time, we have seen a welcome drop in unemployment over the last two months. It is still too early to say whether this heralds the long awaited start of a downward trend. But what we can say with confidence is that since the 1983 election the economy has created a million new jobs and that we have enjoyed continuous employment growth for the longest period for almost 30 years.

Manufacturing industry in the UK is well placed to take advantage of this improved outlook. Manufacturing will benefit particularly from the fuel savings which a lower oil price brings - every \$1 fall in the crude oil price should reduce industrial costs by more than £100 million. At the same time, the substantial exchange rate fall which has accompanied lower oil prices helps to make our goods more competitive in world markets.

But there is one issue on which all industrialists can be guaranteed to make common cause against the Government - the level of interest rates. They are quick to subtract the current inflation rate from banks' base rates and conclude that real interest rates now stand at historically high levels. But I have to say that companies are slower to perform another equally simple calculation and subtract the current inflation rate from the pay settlements they negotiate with their workforce. Yet for every £1 a 1 per cent increase in interest rates adds to firms' pay bills, 1 per cent on pay adds around £4.

And that is why as long as employers in this country continue to pay their workers increases in earnings three times as high as their competitors overseas, their pleas to the Government to reduce industrial costs through cuts in interest rates will carry a hollow ring.



FST

MONEY 86

30/10/86





1985 12/2  
**H. M. TREASURY**

Parliament Street, London SW1P 3AG, Press Office: 01-233 3415  
Telex: 262405

**PLEASE NOTE EMBARGO**

NOT FOR PUBLICATION, BROADCAST  
OR USE ON CLUB TAPES BEFORE  
12.30 PM THURSDAY 30 OCTOBER 1986

30 October 1986

**PERSONAL EQUITY PLANS AT THE MONEY 86 SHOW**

Attached are extracts from the speech by the Financial Secretary to the Treasury, the Rt Hon Norman Lamont MP, at today's opening of the Money 86 Show at Olympia.

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131/86

**NOTES FOR EDITORS**

The Personal Equity Plan scheme was announced by the Chancellor in this year's Budget. It is intended to encourage individuals to invest directly in British industry.

A number of exhibitors at the Money 86 Show are launching Personal Equity Plan schemes from 1 January 1987.

The main features of the scheme are as follows:-

- individual investors resident in the UK can subscribe up to £2,400 a year (or £200 a month), through a registered plan manager, for a direct holding of shares in UK companies listed on the Stock Exchange or on the Unlisted Securities Market. Within the £2,400, up to £420, or 25 per cent of the subscription if greater, may be invested in unit trusts or investment trusts.
- all reinvested dividends on the shares, and all capital gains made on them, will be entirely free of tax, provided the shares are held in a plan for a short qualifying period.

A Treasury leaflet describing the scheme is obtainable from Inland Revenue local offices or from the Treasury.



One of the fundamental aims of this Government has been to encourage people in their desire to be independent - to make their own decisions and stand on their own feet. This includes making their own savings decisions.

As the Chancellor of the Exchequer pointed out in his Budget Speech this year, we have already made Britain a nation of house owners. Now we want the British people to become a nation of shareholders as well.

Over our period in office, we have brought in more and more measures which have encouraged wider share ownership. Our privatisation programme has been and continues to be an outstanding success. Next month, shares in British Gas will go on sale. Next year British Airways, Rolls Royce and the British Airports Authority will go into the private sector.

And the tax system has already encouraged widespread individual shareholding through employee share schemes and the Business Expansion Scheme.

But we wanted to do more to encourage the spread of popular capitalism. That is why, in his Budget this year, the Chancellor introduced the Personal Equity Plan. Its purpose is to encourage direct investment in UK equities.

Let me tell you how the new scheme will work and why we are confident it will succeed.

Starting next January anyone over eighteen years of age who is resident in the UK will be able to put their savings into a new Personal Equity Plan.

Under this scheme individual investors can subscribe up to £2,400 a year or £200 a month and their money will be used to give them a direct holding in UK equities.



In return they will receive generous tax relief. All reinvested dividends on their shares, and all capital gains on them, will be entirely free of tax. The only condition is that the shares are held in the plan for a short qualifying period.

The tax advantages have been specifically designed so that the longer the investor keeps his money in the plan, the greater the tax benefit he gets.

Because we are going to be giving substantial tax relief there will be some rules about what can be held in a PEP. For example, it would undermine the intention of the scheme completely if a PEP were able to consist virtually permanently of cash, rather than shares.

But we have kept things as straightforward as possible for investors, particularly new investors.

They will be simple because:-

- it will be the plan manager, and not the investor who will have to claim the tax relief;
- there will be no capital gains tax calculations;
- there will be no need for the investor to keep any records for the Inland Revenue;
- in fact, as long as the plan is kept intact during the qualifying period, there is no need for the investor to declare his PEP to the Revenue at all.

On the other hand, the scheme is designed to strengthen the link between the investor and the companies he invests in. All or a major part of the investment must be held directly in shares.



So the investor will be able to follow the progress of his shares in the financial press. He will receive copies of the companies' annual report and accounts. And he will have the opportunity to attend shareholders' meetings and use his shareholders' right to a vote.

Personal Equity plans must and will be attractive to investors. But plan managers are important too. People will be looking to them to provide the facilities for investing in this exciting new venture.

That is why we gave potential plan managers every opportunity to feed in views as we designed the details of the scheme.

We have deliberately set out to ask all those who might wish to become plan managers to give us their ideas. We have listened carefully to what they have told us.

For example, some pointed out that our limits on cash in the first year of a plan were too inflexible. We looked at this and decided to make a change.

Now the only restriction on cash holdings in the year a plan is started will be the overall subscription limit of £2,400.

It is important that investments are made at the right time. This change will make this easier.

Some wanted investors to be able to put all their plan money into unit or investment trusts. But this would not give the investor the direct stake in the success of specific companies, which we want to see. That is why we have restricted the amount of this sort of holding to £420 or 25% of the annual subscription, whichever is the higher.



The choice of shares in which to invest will be for the investor and his plan manager. They are free to invest in any ordinary shares in UK companies listed on the UK Stock Market. In the light of the powerful arguments from the Stock Exchange we have also decided that UK ordinary shares on the second tier, the Unlisted Securities Market, will qualify. This will give an even greater choice of companies in which to invest.

The importance of the PEP scheme can be gauged from the interest which has been shown in it. A wide range of people have shown interest in becoming plan managers, from small specialised dealers to major high street institutions. We have also made it possible for building societies to take part.

Already advertisements are appearing from prospective managers, designed to interest old and new customers in their proposed plans.

We have deliberately avoided making any rules on how managers will levy their charges. But we have made it clear that subscribers must be told exactly how their fees will be calculated. So competition for investors' money will be active and fair.

For many investors this will be their first introduction to the Stock Market.

Some will doubtless wish to choose for themselves the shares they wish to invest in.

But others may not wish to take such an active role.

Plan managers will be able to offer them experience and guidance in the form of a discretionary scheme. In this case the investor will leave the choice of initial investment and subsequent management of the portfolio to his manager.



Many people have in the past been discouraged from investing on the Stock Exchange by the tax they would have to pay, and the complications in making returns to the Revenue.

Now, through the PEP scheme, they will be able to keep what they make, and not even have to declare it to the Inland Revenue. It is difficult to think of a more effective measure that this or any Government could have introduced to help investors.

### Conclusion

From the interest shown so far, I am confident that from January next year potential investors will be offered a wide choice of different Personal Equity Plan schemes. This will give a significant new boost to share ownership in this country.

This is a period of change and opportunity. Any investment in drawing the attention of the British public to the advantages of share ownership will, I am confident, reveal a major new market waiting to be tapped.

The Government have created a healthy interest in popular capitalism. This can benefit not only the individual investor, but also British industry and the country as a whole.