PREM 19/717

PART 19 ends:-

draft press statement of 15/7/82

PART 20 begins:-

CST ~~to~~ PM talk of 15/7/82

TO BE RETAINED AS TOP ENCLOSURE

Cabinet / Cabinet Committee Documents

Reference	Date
CC(82) 13th Conclusions, Minute 5	1.4.82
C(82) 28	8.7.82
C(82) 29	8.7.82
CC(82) 38th Conclusions, Minute 5	15.7.82

The documents listed above, which were enclosed on this file, have been removed and destroyed. Such documents are the responsibility of the Cabinet Office. When released they are available in the appropriate **CAB** (CABINET OFFICE) CLASSES

Signed C M Wayland Date 21 August 2012

PREM Records Team

Econ Pol.

PUBLIC EXPENDITURE

As is usual at this time of the year, the Cabinet today began its discussion of public expenditure in the next two financial years. The discussion set the framework for the examination of programmes that will continue through the summer, with a view to decisions in the autumn.

15 July 1982

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PUBLIC EXPENDITURE TO 1985-86

OPTIONS FOR REDUCTIONS

1982 Report by the Public Expenditure Survey Committee

July 1982

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PUBLIC EXPENDITURE 1983-84 TO 1985-86

1982 REPORT BY THE PUBLIC EXPENDITURE SURVEY COMMITTEE

OPTIONS FOR REDUCTIONS

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SUPPLEMENTARY ANALYSIS

A. Options for reductions, by Department and economic category

2. FCO - Overseas Development Administration

Options for reductions and offsetting savings £ million cash

	1983-84	1984-85	1985-86
Offsetting savings		(See text)	
Options for reductions	(2%)	(3%)	(4%)
Net aid programme	20.3	32.0	44.4
CDC	0.3	0.4	0.6
Overseas aid administration	0.5	0.7	1.0
Other external relations - superannuation		(See text)	

Overseas aid

The net aid programme has been reduced by 21 per cent in cost terms between the peak of 1978-79 and 1982-83, compared with an increase of 5 per cent for the rest of public expenditure. (This decline was but marginally offset by the introduction of commercial borrowing by the CDC, which does not score as aid.) Economic circumstances permitting, and without time-limit, the UK is committed to the UN target for aid of 0.7 per cent of GNP. On present plans however we will move further away from this target, scoring 0.32 per cent in 1984-85 compared with 0.38 per cent in 1981-82. The reductions made in the UK programme, against a background of demands for increasing aid (eg at the Cancun summit) have led to domestic and international criticism. There are signs of pressure for more aid impinging upon our political and commercial relations with individual countries, as witness recent dealings with India and Malaysia.

2. Rising and inescapable multilateral commitments mean that the brunt of past reductions have fallen on our bilateral programmes (down 36 per cent in cost terms between 1978-79 and 1982-83), contrary to the Government's aid policy, announced in February 1980, which seeks to give greater weight to bilateral expenditure. Forseeable demands for bilateral aid are numerous, including pressure from major Commonwealth recipients for the restoration of our aid to its past levels; requests for urgent balance of payments support from countries in which British interests are

involved (eg Turkey, Jamaica, several African states); humanitarian help for refugees; and aid expenditure to help secure contracts of particular industrial and commercial significance to the UK.

3. Because a significant proportion of bilateral aid is not yet finally committed over the next few years there is no technical problem over securing reductions. But the options for reductions would mean further reductions in bilateral aid of 3.8 per cent, 5.9 per cent and 7.5 per cent in 1983-84, 1984-85 and 1985-86 respectively, intensifying the undesirable effects noted above.

Overseas aid administration

4. Manpower numbers have fallen by 14 per cent between 1979 and 1982 and are planned to reduce by a further 9 per cent between 1982 and 1986. In ODA's view, further reductions in the financial provision for the programme would mean cutting out functions essential to the efficient administration of the overseas aid programme.

Other external relations (part) - superannuation

5. This programme consists of various pensions supplements to which the pensioners concerned have a statutory entitlement derived from the Pensions Increase Act. The required provision depends wholly on the decisions to be taken on the future levels of UK public sector pensions generally (see eg civil superannuation, chapter 23). Hence no options for reductions are shown.

Crown Agents

6. This programme consists of receipts from repayments of debt. Options for reductions (ie increased receipts) are not feasible.

Commonwealth Development Corporation

7. The certain political outcry which would result from a partial withdrawal of the permission given to the CDC to borrow commercially in 1983-84 and 1984-85 would not be worth the savings secured. Options for reductions would therefore have to be financed by a reduction in overseas aid. A reduction in the CDC baseline figure for 1985-86 could in principle be secured; Ministers have yet to consider whether and what amount the CDC should be allowed to borrow in that year.

3. Foreign and Commonwealth Office - Other

Options for reductions and offsetting savings £ million cash

	1983-84	1984-85	1985-86
Offsetting savings required	14.3	9.4	12.8
Offsetting savings			
Overseas representation	11.1	6.1	7.4
Overseas information	3.2	3.3	5.4
Options for reductions	2%	3%	4%
Overseas representation	9.4	14.1	19.5
Overseas information	-	0.5	1.0
Other external relations	0.5	0.7	0.7
Military aid	0.3	0.4	0.5
Total	10.2	15.7	21.7

Overseas representation

A cut of the order indicated in overseas representation would entail staff reductions, post closures and/or delay in implementing building projects abroad (possibly incurring greater costs in the longer term). Of this cut approximately £5.0 million would be in respect of the additional bid for the British Antarctic Survey. (This bid will be subject to consideration by OD Committee). If the options for reductions were included, further cuts of between £9.4 million and £19.5 million would give rise to Parliamentary and national concern (eg over closure of Missions).

Overseas information

2. If the additional bid had to be found from within the planned level of expenditure on the BBC External Services, cuts in vernacular services and curtailment of monitoring of foreign broadcasts would ensue. Such cuts would encounter strong public and Parliamentary opposition. Under the options for reductions the British Council

would have to reduce staff or withdraw representation from some countries. There would be strong protests from the Council's supporters in Parliament and elsewhere.

Other external relations

3. The major part of this expenditure is on internationl subscriptions (£68.6 million of £77 million 1983-84). Unilateral withdrawal from the bigger organisations (Council of Europe, Commonwealth Secretariat, Western European Union) would give rise to substantial international criticism. Ministers have already approved a policy whereby savings should be found by seeking real reductions in the expenditure of international organisations wherever possible: however, this cannot be expected to lead to significant savings within the period covered by the survey.

4. In practice, therefore, savings in this area would be likely to take the form of reduced unilateral grants to various non-governmental organisations, and/or for scholarships etc and/ or on miscellaneous services. The relatively small sums involved could cause disproportionately damaging rows (eg within the Commonwealth, if the Commonwealth Institute, or scholarships, were to be cut).

Military aid

5. The only option would be to reduce the level of training assistance for overseas governments.

(No legislation would be required to implement these cuts).

5. Intervention Board for Agricultural Produce

Options for reductions and offsetting savings

1. Most of the Board's expenditure is mandatory under EC Regulations and is not subject to direct UK control. Most schemes are also 100 per cent financed from the EC Budget; and hence to the limited extent that expenditure could be reduced by UK actions any public expenditure saving would be largely offset by reduced receipts under programme 2.7.

2. For these reasons it would not be appropriate to show offsetting savings to cover the net additional bid.

3. Equally there is virtually no scope for option reductions in the programme. The one major exception is the beef premium scheme which is operated only in the UK and which was, until the 1982 CAP price fixing, only 25 per cent financed from the EC Budget. Ministers considered the possibility of ending the scheme in the 1981 survey and decided then not to pursue this option. Subsequently the scheme was renewed for 1982-83 in the 1982 price fixing, but with the proportion of EC financing raised to 40 per cent. Any net savings from ending the scheme would consequently be reduced.

6. Ministry of Agriculture, Fisheries and Food

Options for reductions and offsetting savings

£ million cash

	1983-84	1984-85	1985-86
Offsetting savings required			
(a) Agriculture fisheries & food	7.6	9.7	22.0
(b) Thames tidal defences	1.5	3.5	-
Options for reductions required	17.0	25.1	35.6
Items			
(a) Agriculture Fisheries & Food			
(i) estimating reductions	8.4	10.2	21.8
(ii) deferment of agreed AHDS target income option	1.2	2.0	2.1
(iii) land sales	-	1.2	-
(iv) reductions in capital grants	17	25	35
(b) Thames tidal defences	-	-	5.2

Offsetting savings

1. To meet the cost of the bid for a central marketing organisation Agricultural Ministers have already offered to defer implementation of a reduced target income for applications under the Agriculture and Horticulture Development Scheme (AHDS). The Departments also propose that the land sales programme should be rephased to take account of planned disposals that were not completed in 1981-82. Together with the reduced estimating requirements these savings offset in full the additional bids set out in the PESC report, although the Agricultural Departments do not accept the need for increases on the Thames tidal defences to be offset by savings on agriculture, fisheries and food.

Options for reductions

2. Given the nature of the Agricultural Departments' expenditure and their statutory, EC and other policy responsibilities, it is not feasible to make cuts on all parts of their expenditure which are of the required level (£17.0 million in 1983-84 rising to £34.8 million in 1985-86). For example deferment or abandonment of work on the Thames tidal defences would result in unacceptable risks to human life and property.

3. In the view of the Agricultural Departments, the savings options could be achieved only by cutting back direct support for agriculture and fisheries, arterial drainage and extra-mural R & D. If the full reductions were achieved in any one of these areas they would imply cuts by 1985-86 of:

(a) 11 per cent in support for agriculture (principally capital grants and hill farming);

(b) 50 per cent in support for fisheries;

(c) 50 per cent in arterial drainage;

(d) 50 per cent in extra-mural R & D.

4. The Agricultural Departments consider that these options, applied either individually or in some combination such as that in paragraph 6, would imply:

(a) A further fall in capital investment and consequent effects on productive capacity; and risks to hill farming viability.

(b) Damage to an industry already facing serious difficulties.

(c) Endangering the programmes of the water authorities.

(d) Disruption of the long-term planning of research programmes, with probable redundancies and adverse effects on agricultural productivity.

5. For the purpose of this paper the Agricultural Departments have put forward an illustrative option which assumes that the specified reductions would be achieved entirely through a cut back in capital grants. Changes would in the main have to be made to the national scheme (AHGS) because under the EC scheme (AHDS) a large

proportion of expenditure is committed. Cuts of up to one-third in the standard rate of grant for all items and of nearly one-third in the less favoured area (LFA) rate of grant for drainage would be necessary; and in addition it would be necessary to cease assistance for grassland regeneration and land reclamation outside the LFA. The overall effect would be to reduce the standard rate of grant in the scheme from 22½ per cent to 15 per cent (except for drainage - 37½ per cent to 25 per cent). Secondary legislation would be necessary and there might be some small savings in manpower. Cuts of this kind would, in the view of the Departments, lead to a further fall in investment which has already declined with very damaging effects, and for that reason would be unacceptable to them.

6. The Treasury recognises that it is primarily for the Agricultural Departments to consider the ranking of possible option cuts; and notes that the Departments have chosen to express the cut as one falling entirely on capital grants. The Treasury points out, however, that if cuts were to be spread more evenly across the programme the impact on any one area of expenditure could be much reduced and the option percentages could be achieved by a package involving:

(i) Support for agriculture:

- reductions in average capital grant rates under the national scheme (but not the EC scheme) of around one-fifth.
- withdrawal of the discretionary Exchequer financed supplement to the mandatory EC-financed subsidy to suckler cow herds;

(ii) In-house and extra-mural research

- reductions rising to 7 per cent by 1985-86.

(iii) Arterial drainage

- reductions of about 4 per cent.

7. Forestry Commission

Options for reductions and offsetting savings £ million cash

	1983-84	1984-85	1985-86
Offsetting savings required	-	-	0.9
Options for reductions required	1.3	1.9	2.6
Total	1.3	1.9	3.5
Items identified in order of acceptability			
1. Timber receipts	-	-	1.2
2. Reduction in vehicles, etc	0.9	0.4	1.6
3. Capital building work	-	0.2	-
4. Materials, services, and admin expenses	0.4	1.3	0.7
Total	1.3	1.9	3.5

1. The Forestry Commission expect timber prices in 1985-86 to be some 2 percentage points higher than the rate assumed in the survey.

2. The reduction in the funds available for the purchase of vehicles and machinery would necessitate some deferment of replacement with the consequential risk of increased repairs and operational costs.

3. Reductions in capital building expenditure will delay the house improvement programme and other developments.

4. Arbitrary reductions in operational costs of machines, purchase of materials and services and in overheads, travelling and subsistence, etc would be imposed.

8. Department of Industry

Options for reductions and offsetting savings	£ million cash		
	1983-84	1984-85	1985-86
Offsetting savings required	290.9	419.4	388.3
Options for reductions required	24.0	30.0	43.0
Total	314.9	449.4	431.3

Offsetting savings

1. Offsetting savings of the magnitude of the total additional bids could only be achieved by drastically cutting RDGs (for example, halving the rate of grant or excluding half of manufacturing industry). Such action would be very damaging to industry and to the regions and would be totally inconsistent with Government assurances about the stability of regional policy. A much smaller cut (£50 million a year) was found impracticable by Ministers in the 1981 survey. Specific offsetting savings are required to meet the additional expenditure of £9 million a year arising from changes in Assisted Areas agreed by Ministers in June 1982. The Department are considering how this might be achieved.

Options for reductions

2. Options for reductions of 2 per cent, 3 per cent and 4 per cent over the PES years (ie about £24 million £30 million and £43 million) might be achieved by:

(a) altering RDGs (a 1 per cent cut might produce savings of £30 million a year), and

(b) cutting back on selective financial assistance (assistance to industry in the assisted areas, assistance to individual industries, industrial R & D and other support).

9. Department of Energy

Options for reductions and offsetting savings £ million cash

	1983-84	1984-85	1985-86
Offsetting savings required	17	19	22
Options for reductions required	10.5	17	23.5
Total	27.5	36	45.5
Offsetting savings			
Nuclear R & D	-	-	7
Non-nuclear R & D) Energy conservation)	17	19	15
Total	17	19	22
Options for reductions			
Nuclear R & D	9.4	15.2	21.5
Non-nuclear R & D	0.5	1.0	1.0
Energy conservation	0.4	0.6	0.8
Departmental administration	0.2	0.2	0.2
Total	10.5	17.0	23.5

Options for reductions

In the event of a lower level of percentage options, the reductions would need to be reviewed, but would probably be applied pro rata to the table above, with the reductions continuing to be weighted on nuclear R & D.

2. Although half of the baseline consists of social grants to the coal industry, it is not feasible to look to that area of expenditure for any contribution to option reductions since the expenditure is demand-determined (depending on progress with pit closures) and subject to inescapable political commitments. The reductions would have therefore to be found entirely from unrelated areas, mainly energy research and development and energy conservation. The effects would be as described below.

Nuclear R & D

3. On top of the reduction of 8½ per cent in nuclear R & D in last year's survey, further cuts of this size would almost certainly be achievable only by enforced redundancies. To offset the extra short term costs of redundancy (as opposed to voluntary early retirement), reductions in manpower would have to be disproportionately large. Due to the lack of flexibility with which such a policy could be carried out, it is not possible to predict precisely which programmes would be most severely affected. However, the fast reactor programme (which constitutes half of the net expenditure of the Atomic Energy Authority) would be bound to be severely affected, for example in the areas of fuel and fuel reprocessing development and of development work for a Commercial Demonstration Fast Reactor. This would harm the current negotiations on international collaboration, reduce the prospects for securing a satisfactory agreement and set back implementation of the options for the fast reactor which Ministers might decide to adopt. Other likely effects would be:

(a) damaging the role of the Culham fusion laboratory in support of the Joint European Torus (JET) project and in the fusion research programme co-ordinated with other members of the EC;

(b) reductions in the Authority's nuclear R & D capability as a whole and the preparation of its radioactive waste for long-term storage or disposal;

(c) cuts in capital and maintenance programmes, with the risk that ageing, important facilities may have to be closed on safety grounds;

(d) possibly affecting work on the longevity of advanced gas-cooled reactors and on safety work on the pressurised water reactor;

(e) a risk of serious effects on employment in certain areas especially in Caithness.

Non-nuclear R & D

4. Following last year's survey further cuts would have a serious effect on a budget which is already too small to sustain programmes in which the Department would wish to be active. Further reduction would have to be made in work on offshore geology which is important to the formation of depletion policy and to negotiation of licences

with oil companies. In the field of renewables R & D, work on biofuels and solar energy would have to be run down more quickly.

Energy conservation

5. The reduction would fall on one or more of the programmes which provide information or advice or which stimulate energy savings projects, particularly in industry.

Offsetting savings

6. Although the greater part of the additional bids would not form part of the NCB's external finance (since payments under the Redundant Mineworkers Payments Scheme are made direct to beneficiaries), nevertheless the expenditure is in support of the coal industry. In the Department's view the bids should therefore be taken into account (together with the additional amounts that will be required for operating and deficit grants) in considering in the Investment and Financing Review how much finance should be allocated to support for the industry.

7. If, however, offsetting savings were required from the Department's other expenditure programmes further savings would be sought from nuclear R & D. But due to the offsetting costs of large-scale enforced redundancies and of rendering closed laboratories safe it seems unlikely that the AEA would be able to show net reductions in expenditure, over and above the percentage reductions, before 1985-86. If this proved to be the case, the Department would for example have to resort to drastic interruptions and delays in offshore technology and renewable energy (wind, geothermal, solar etc) R & D programmes and in energy conservation. Expenditure on these programmes would have to be reduced by over one-third. This would result in cancellation of contracts, incompleted work and dispersal of teams of experts. It would be bound to have major political repercussions and require very careful consideration.

10. Department of Trade

Options for reductions and offsetting savings

£ million cash

	1983-84	1984-85	1985-86
Offsetting savings required	2.7	-	7.6
Offsetting savings proposed by Trade	-	-	-
Offsetting savings proposed by Treasury:-	3.0	6.0	13.5
(a) Elimination of ECTMO* provision	-	-2.6	-2.6
(b) Withdrawal of bids:-			
(i) Tourism (promotion and BTA exchange losses)	-1.2	-1.3	-1.4
(ii) Export promotion	-	-	-0.1
(iii) Trade co-operation	-0.1	-0.1	-0.2
(iv) Consumer protection (part)	-0.4	-	-
(v) Standards (part)	-	-0.1	-0.4
(vi) Departmental administration (part)	-0.2	-0.1	-
(vii) Shipping services (civil hydrography)	-1.1	-1.8	-8.8
(b) Total	-3.0	-3.4	-10.9
(a) and (b) Total	-3.0	-6.0	-13.5

*European Community Trade Mark Office

The Department of Trade has proposed no offsetting savings for their net additional bids of £2.7 million in 1983-84 and £7.6 million in 1985-86 because virtually the entire excess is attributable to the additional bids for civil hydrography: £2.0 million in 1983-84 and £9.0 million in 1985-86 - a programme which had been carried on the Defence Budget, and which is still the subject of dispute.

2. The Treasury takes the view that many of the additional bids are inappropriate and should be withdrawn and the costs of others should be absorbed within the programme. The Treasury also considers that the provision of £2.6 million a year from 1984-85 onwards on the protection of innovation programme for the furnishing of an headquarters building in the UK for the European Community Trade Mark Office

should be eliminated. Although Ministers have agreed to seek the siting of the ECTMO headquarters in the UK, this was on the basis that there should be no Exchequer cost. The Treasury's proposals would allow for the acceptance of the most essential and politically sensitive bids.

Options for reductions

	1983-84	1984-85	1985-86
	2%	3% (approx)	4%
Required options for reductions	5.2	8.0	11.0

3. Options for reductions have been calculated on Cmnd 8494 totals as adjusted for the change in the National Insurance Surcharge less Civil Aviation Authority's National Loan Fund and foreign borrowing and issues of Public Dividend Capital to British Airways. These programmes are dealt with in the nationalised industries context.

4. In the Department's view reductions at the levels stipulated would be impracticable. Many of the Department's services are of a regulatory nature and are imposed by statute (for example Patents, Insurance, Companies, Insolvency, Marine and Civil Aviation Regulations etc) and these cannot be offered as options unless legislation to reduce the Department's responsibilities in these areas is regarded as a realistic possibility. Moreover a substantial proportion of the costs of these services is already recovered in fees and charges. Subscriptions to international bodies such as GATT, IMCO and ICAO are fixed by international agreement and cannot be cut without breach of the UK's obligations.

5. The Department points out that any reductions would need to be concentrated on its narrow range of discretionary expenditure in the areas of export promotion, tourism, other grants in aid or shipping services. The attainment of the option levels would call for decisions on the following lines:-

Export Promotion

6. The Department believes that there is no scope for further increase in fees and charges and that consequently an option cut would have to come entirely from reduced provision. This would be for the British Overseas Trade Board (BOTB) to apply to the various services which the Department runs under its supervision. The Board and its

Chairman would react very strongly against any proposals for cuts: the BOTB programme was cut last year and in 1979. Although there has been a history in recent years of consistent underspends against provision the Department and the Board consider that this is attributable to the worldwide business recession and that the level of provision would be too low if there were to be an upturn in economic activity in the near future.

Tourism

7. Tourism is the Department's only other major area of discretionary programme expenditure. In contrast with Export Promotion the provision is normally fully spent. Responsibility for the support of tourism is shared with Scotland and Wales who include it in their respective block budgets; the BTA acts on behalf of all three countries. Cuts would involve either a reduction of Section 4 support for selected tourism projects (with job losses in the public and private sector) or reductions in the British Tourist Authority's and the English Tourist Board's promotional activities (which would also lead to job losses and to losses of matching trade contributions to the organisations). The Department considers that cuts here should, if they are made at all, be matched by the Scots and Welsh.

National Association of Citizen's Advice Bureaux (NACAB)

8. Cuts in the NACAB grant in aid would mean reducing the staff, and thus the local activity, of this body. The recession continues to place pressures on the CAB services. There is concern about maintaining the quality of the assistance offered by NACAB. Implemention of a cut in this area would be politically sensitive.

Shipping Services

9. A considerable amount of the Shipping Services expenditure is devoted to regulatory services imposed by statute. Option reductions could therefore only relate to certain marine safety expenditure not specifically covered by statute -the coastguard service, research and development on marine safety and pollution. Public criticism of cuts in these areas could be substantial. They would be seen as economy measures imposed without regard to safety and there would be oppostion in coastal constituencies.

Local authorities current expenditure on consumer protection

10. The Department point out that they have little control over this area of the programme but option cuts would require local authorities to make savings of £1.2 million in 1983-84, £2.0 million in 1984-85 and £2.5 million in 1985-86.

A possible package

11. A package to meet the requirement to identify options could be as follows:

£ million cash

	1983-84	1984-85	1985-86
(a) Export Promotion: programme cut to be allocated by BOTB	2.0	3.0	4.0
(b) Tourism: reductions in Section 4 assistance and/or in BTA and ETB's promotional efforts	1.0	1.5	2.25
NACAB reductions in grant in aid	0.5	0.75	1.25
Shipping Services	0.5	0.75	1.0
Local authority current expenditure on consumer expenditure	1.2	2.0	2.5
Totals offered	5.2	8.0	11.0

11. Export Credits Guarantee Department

Options for reductions and offsetting savings £ million cash

	1983-84	1984-85	1985-86
Offsetting savings required	214.6	-	-
Options for reductions required*	3.7	-	-
Total	218.3	-	-
Items			
1. Raising of fixed rates under the Consensus	28.8	35.6	43.4
2. Yen facility	3.7	4.5	5.6
3. Refinance	50.0	-	-
4. Withdrawal of matching facility	5.4	5.7	5.9
Total	87.9	45.8	54.9

*Percentage reductions are covered by reduced requirements in 1984-85 and 1985-86.

The demand-determined nature of ECGD's programmes and the expenditure variations resulting from economic factors once commitments to provide specific facilities have been made limits the scope for savings on ECGD's programmes.

2. Possible savings could result from:-

(i) raising the fixed rates of interest;

(ii) the provision of a new yen denominated export credit facility;

(iii) increasing the share of outstanding refinance held by the private sector; and

(iv) withdrawing the mixed credits matching facility.

3. Over the survey period savings may result from studies to be completed by ECGD on possible methods of savings on interest support costs and from any multilateral increases in interest rates for fixed rate export credits agreed under the International Consensus. Savings may also arise from the introduction of a new yen denominated

export credit facility: this facility is likely to attract less interest support costs due to the lower differential between market rates and the various interest rates applicable for export credits in yen and the major alternate currencies currently utilized. However the extent of potential savings from changes in the Consensus and the provision of the yen facility can neither be readily gauged nor directly controlled.

4. A further increase in the private sector's share of outstanding refinance (approximately £500 million) would increase the receipt levels for the current and future two years, and would constitute a reduction in public expenditure. It is not however clear that that the banks or other private sector institutions would be prepared to co-operate. Apart from this such transfers would have adverse implications for monetary management.

5. When the introduction of the mixed credits matching facility was announced in Parliament it was stated that it would be reviewed in the second half of 1982 or sooner if there is significant progress internationally in restricting soft credits. To date the facility has not been utilized.

12. Department of Employment

Options for reductions and offsetting savings

	£ million cash		
	1983-84	1984-85	1985-86
Offsetting savings required	-	23.5	-
Options for reductions required	33.4*	87.7	6.7*
Total	33.4	111.2	6.7
Items			
(a) Reductions within the MSC	29.4	49.4	6.7
(b) Reductions within the HSC	1.8	2.8	-
(c) Reductions in the Community Enterprise Programme	2.2	-	-
(d) Reduction in rebate to employers from the redundancy fund:			
- from 41 to 36 per cent	-	24.5	-
- from 36 to 39 per cent	-	34.5	-
Total	33.4	111.2	6.7

*Net of reduced requirements

The table above records the offsetting savings and the effects of reducing the baseline by 2 per cent in 1983-84 rising to 4 per cent in 1985-86.

2. The additional bids can be met from reduced requirements in 1983-84 and 1985-86, but not in the intervening year. The bulk of the reduced requirements are estimating changes arising from revised assessment of the costs and demand upon certain of the special measures. Much the largest reduction in each year relates to the Job Release Scheme. The savings in this scheme reflect lower than expected take-up from the reduction of age limits for men to 63 in 1981 and 62 in 1982; and an assumed revision, consistent with existing policy, to age 64 entry from April 1984.

3. In 1984-85 reduced requirements fall short of additional bids by £23.5 million. If the Department itself was obliged to find such a sum it believes it would have to

reduce the rebate to employers from the redundancy fund. A reduction from the existing level of 41 per cent to 36 per cent in 1984 only would secure £24.5 million. This would impose an equivalent additional burden on employers making redundancies, but employers generally would eventually benefit from a lower rate of contribution to balance the fund.

4. Other option reductions at the levels suggested would mean that the programmes of the Manpower Services Commission (MSC) and the Health and Safety Commission (HSC) would have to bear a share of the burden. The Department emphasises that the size or distribution of any reductions in these programmes would have to be agreed with the two Commissions who have yet been consulted. Illustrative reductions are put forward by officials but these might be subject to change should any question of implementation arise.

5. Options within the MSC programme, with a broad indication of savings in 1983-84 and 1984-85, are:

		£ million cash	
		1983-84	1984-85
(a)	Slow down of the job centre programme and of the rebuilding of employment rehabilitation centres, some local office closures and abolition of grants payable to single non-householders under the employment transfer scheme. Economies in telecommunications	4	5
(b)	No uprating of YOP/YTS allowance	15	33
(c)	Minor reductions in support services	1	1
(d)	Employment service savings from Rayner scrutiny (not yet considered)	3	6
(e)	Extra receipts from direct training services and savings in resources at skill centres	4	3
(f)	Limited uprating of TOPS allowances	2	1

6. Most of these items would have consequential effects in 1985-86 amounting, in total, to considerably more than the £6.7 million which is shown in the main table as being necessary in that year.

7. Options suggested for the HSC are:

(a) increases in current fees and charges and the introduction of new charges for existing services

(b) cut-backs on major research projects, both intra and extra mural

(c) reductions in capital expenditure on buildings and equipment

(d) minor reductions in spending on equipment and stores.

8. Should the Department be pressed further to meet the cost of all the additional bids as well as a 2 per cent cut in the baseline, the balance of £2.2 million in 1983-84 would be found from a reduction during the year in the Community Enterprise Programme, possibly entailing up to 1000 places (around 3 per cent of total places). In 1984-85 some £34.5 million would be needed. This could be found from a further reduction in the rebate to employers from the redundancy fund. The level of 36 per cent mentioned in paragraph 3 would need to be brought down further to 29 per cent with the consequences already described. A reduction to 29 per cent would require main legislation. Subordinate legislation would secure a change to 35 per cent.

9. All the reduced requirements shown in the main table are current expenditure. Of the other offsetting savings and otpion reductions, current expenditure accounts for around 94 per cent in 1983-84 and 97 per cent in 1984-85.

13. Department of Transport

Options for reductions and offsetting savings £ million cash

	1983-84	1984-85	1985-86
Offsetting savings required	35	32	32
Options for reductions required	86	134	185
Total	121	166	217
Items			
Capital spending			
A Motorway/trunk road construction	33	44	59
B Local transport	36	49	64
Central government subsidies to transport industries			
C British Rail	39	58	79
D Other	1	2	3
E Ports	7	6	7
Miscellaneous			
F Driver and Vehicle Licensing Centre	3	4	5
G Other transport services	2	3	5
Total	121	166	217

1. To offset the additional bids (£35 million in 1983-84; £32 million in 1984-85; £32 million in 1985-86), excluding any increased provision for local authority current spending, and to achieve required reductions (£86 million in 1983-84; £134 million in 1984-85; £185 million in 1985-86) the Department is required to identify means of reducing expenditure by £121 million in 1983-84; £166 million in 1984-85; £217 million in 1985-86. As noted in paragraph 19 of the main text the Department points out that Ministers have decided that local authority current expenditure will be considered in a separate self-contained block. In their view it follows that local authority current expenditure should not be included in the overall figures for this programme on which percentage reductions are illustrated and the above figures should be reduced by one third.

2. The above table shows how using the grand totals, reductions could be allocated between Departmental programmes proportionally. Consideration of specific options

for local transport - eg restrictions on concessionary fare schemes in public transport; removal of the obligation to maintain unclassified roads, both of which are controversial and require primary legislation - may need to be resumed when decisions on the aggregate of local authority current expenditure have been made.

3. No options for reduction are shown for the motorway and trunk road maintenance programme, or British Rail pensions, on which there are significant additional bids.

Sifting of options

British Rail (C)

4. As explained in the main text, a review is being undertaken of BR's deteriorating finances and, in the meantime, the baseline reflects a working assumption that grant is paid in the later years at the level set for 1982. It is not possible to assess the effects of particular options for reductions in advance of the review coming to a conclusion.

Ports (E)

5. Subsidies to Port of London Authority and the Mersey Docks and Harbour Company are being reduced over the survey period as quickly as possible. Port investment is at an historically low level at present and while some underspending is possible, an upturn in economic activity could create pressure by the ports to increase their commercial investment.

Other transport industries (D)

6. £1 million per year could be found from the National Freight Company's travel concessions grant.

Miscellaneous expenditure
DVLC (F)

7. The only options identified for DVLC, who perform a tax-gathering function different in character to the work of the rest of the Department (£80 million of expenditure in 1982-83 supporting the collection of about £1,850 million in vehicle excise duty) involve radical changes in policy, such as the abolition of driving licenses

or VED the latter with matching increases in petrol tax, which has been recently rejected by Ministers. The Department would however regard as unacceptable additional cuts in other programmes, such as construction, to protect this function.

Other (G)

8. £1 million per year could be found from reduced capital spending on driver and vehicle testing schemes. Any further contribution would have to be found from research expenditure, both intra and extra mural, which is presently the subject of a joint review by Treasury and DTp.

Capital spending (A and B)

9. This means that the great bulk of reductions, both to offset additional bids and to make option reductions, would have to come from capital spending. There are virtually no savings available on public transport investment, which is at a minimal level at present, so the only available candidates are the road construction programmes of both central and local government.

Motorway and trunk road construction

10. As explained in paragraphs 8 and 9 of the main text the volume of road construction work which can be carried out within any level of provision depends crucially on the movement of prices. The proportional cut of about £33 million in 1983-84 would be within the possible range of price movements in the programme, although it would probably reduce by about half the money available for new starts. Given the uncertainties about price forecasts it is not possible to forecast accurately the effect on future years; but in DTp's view the cash provision for future years may prove insufficient to maintain current levels of output against the expected rise in prices.

Local roads

11. The proportional cut would have a similar effect on the local authority roads programme. A cut of £36 million in 1983-84 would mean a cut of about 20 per cent in the cash available for new road schemes, and a substantial reduction in the bypass programme.

14. Department of the Environment - Housing

Options for reductions and offsetting savings

	£ million cash		
	1983-84	1984-85	1985-86
Offsetting savings required	980	825	630
Options for reductions required	55	86	119
Total	1035	911	749

1. The reductions required to provide savings of 2 per cent in 1983-84, 3 per cent in 1984-85 and 4 per cent in 1985-86 on the existing baseline are shown above. These can be met to a large extent by the reduced requirements arising from interest rate forecast changes (paragraphs 8 and 9 of the main report). These are £52 million, £46 million and £200 million for 1983-84, 1984-85 and 1985-86 respectively.

2. The offsetting savings required result from the Department's bid for £980 million additional capital expenditure in 1983-84, with the corresponding increase for future years (paragraph 6 of the main report). For 1983-84, the reduction could only be achieved by further increases in rents. The rent increase required would be an average of almost £8 per week. The Department regards this as impossible and undeliverable. For 1984-85 the existing baseline allows capital provision to increase over the 1983-84 baseline by more than prices even if rents rise in line with prices. The savings in 1984-85 could therefore be achieved without a fall in output from capital expenditure. A rent increase in 1983-84 sufficient to provide the required offsetting savings would also provide more than enough offsetting savings in the later years.

15. Department of the Environment - PSA

Options for reductions and offsetting savings

£ million cash

	1983-84	1984-85	1985-86
Offsetting savings required	20.3	28.3	25.0
Options for reductions required	8.7	13.6	18.8
Total	29.0	41.9	43.8
Scope for making cuts without affecting contracts already let			
Operational requirements (6 schemes)	1.0	1.8	2.3
Lease expiry (2 schemes)	2.3	3.4	1.6
Overcrowding/increased efficiency (11 schemes)	1.5	3.8	4.1
Total	4.8	9.0	8.0

1. It is assumed that the option cuts are 2 per cent in 1983-84, 3 per cent in 1984-85 and 4 per cent in 1985-86. On the basis of the figures now in the programme this would mean cuts of

£ million cash

1983-84	1984-85	1985-86
8.7	13.6	18.8

However if the cuts are related instead to the net provision to be retained by PSA after repayment is introduced they will be much smaller. It is not possible to say exactly how big they will be but the maximum 1985-86 cut (ignoring the anticipated repayment receipts which will produce a negative PSA programme total) would probably be under £2 million.

2. An option cut based on PSA's residual provision after adjustments for repayment would involve cancelling or deferring three or four major new works schemes to meet Departments' requirements or to replace leased accommodation which cannot continue to be occupied. The scope for making cuts without affecting contracts already let is as set out above.

3. Even cancelling all these major new works schemes could not achieve the figures for cuts on the whole programme before repayment. It would not be acceptable to make cuts on works already in progress and any further savings would therefore have to be found from elsewhere. However PSA does not consider that it would be acceptable to make significant cuts on current expenditure. It is not possible to assume greater savings from a run-down in the size of the estate than that now incorporated in the figures, the increase in money rents is feared likely to exceed the cash allowances and the squeeze on maintenance funds is already causing problems over working conditions.

16. Department of the Environment - Other

Options for reductions and offsetting savings

The Department have failed to produce any offsetting savings. They argue that the only areas for which such savings could be found are those where they are seeking the additional bids. They have also failed to identify any specific options for reductions, merely saying that any options required will come from controlled programmes.

17. Home Office

Offsetting savings

£ million cash

	1983-84	1984-85	1985-86
Offsetting savings			
Police superannuation	32.4	-	-
Prisons	15.8	21.6	15.7
Police civilians	2.0	1.1	-
Fire (cg)	1.3	1.4	-
Civil defence (la)	3.6	4.1	4.1
Total	55.1	28.2	19.8

Other offsetting savings may be found in the continuing scrutiny of detailed central government requirements, but they are unlikely to total more than several million pounds.

Options for reductions

2. The baseline provision is made up as follows:

£ million cash

	1983-84	1984-85	1985-86
Spending authority			
Local authorities	3281	3416	3553
Central government	661	716	745

(a) Local authorities

3. Reductions in current expenditure by the police, courts, probation and fire services could not be delivered, short of taking specific new powers, eg to reduce police establishments or control directly the numbers of police civilians employed by individual authorities.

4. Reductions in capital expenditure on police, probation and magistrates courts building could be delivered, but would be opposed by the Home Office on the grounds that existing accommodation is unsatisfactory and needs are growing. The Treasury believe that a reduction of £10 million a year is feasible.

(b) Central government

5. Central government expenditure is dominated by the cost of the prison service. The savings required to offset extra bids for prisons and to include reductions of 2 per cent, 3 per cent and 4 per cent in the three years would be:

		£ million cash
1983-84	1984-85	1985-86
£55.3	£61.9	£78.8

Marginal savings on prisons expenditure could not achieve anything like these figures. The only practicable way would be to reduce the prison population. Little would be achieved until it was reduced below the certified normal accommodation (CNA), as above that figure reductions would lessen overcrowding without enabling commensurate closures of establishments and staff savings to be achieved. To bring about the savings required the CNA would need to be reduced by about 9 per cent to about 34,000 for the first two years. This would involve the closure of 18 - 20 establishments. For the third year a further reduction to 32,000 would be required, involving the closure of about 5 more prisons.

6. If the prison service were to be exempt, the reduction to be illustrated would represent 6 - 12 per cent of other Home Office expenditure, two-thirds of which is accounted for by police support and central administration. Even pro rata cuts of 2 - 4 per cent would seriously affect the quality and quantity of scientific and technical support for the police and in the training field would be counter to the recommendations of the Scarman report. If further cuts were applied to central administration, they would involve manpower reductions below the agreed Home Office target for 1 April 1984, which would not merely frustrate existing plans for improvements but lead to a significant deterioration in police support, immigration

control and other services, and the risk of breakdown of after entry immigration control altogether.

7. The Treasury, however, believe that certain options are possible which would not be inconsistent with the commitment on law and order. These include a decision to revalue annually at, or close to, the rate of inflation, the level of fixed penalty fines; and similarly to uprate the maxima on all other fines in accordance with powers included in the Criminal Justice Bill. Action might also be taken to improve fine enforcement, and savings made by reviewing the deployment of traffic wardens.

8. In addition, the Treasury believe that losses on prison industries suggest there should be a cut-back in working and fixed capital investment; further savings might be made on vocational training and educational services; and the prison refurbishment programme, which already seems too ambitious for the resources made available, could be trimmed. Minor savings might be achieved by increasing the threshold for payments under the Criminal Injuries Compensation Scheme, either annually or biennially.

18. Lord Chancellor's Department

Options for reductions and offsetting savings

£ million cash

		1983-84	1984-85	1985-86
Offsetting savings required		-	-	40.0
Options for reductions required		9.0	15.1	20.9
Total		9.0	15.1	60.9
Items				
	(A) Court Buildings			
(i)	Postponement of site acquisition and construction starts on new buildings	0.6	1.2	3.0
	(B) Court Services			
(ii)	Reduction of jury from 12 to 10	2.3	2.3	2.3
(iii)	Juries: abolition of peremptory challenges and standing-by	-	1.0	1.0
	(C) Legal Services			
(iv)	Restrict Advice and Assistance to matrimonial and criminal matters	6.5	7.5	8.5
(v)	Rights of audience for prosecuting solicitors in the Crown Courts	-	0.8	0.8
(vi)	Separate but fair remuneration for matrimonial legal aid	-	2.0	2.0
(vii)	Withdraw criminal legal aid for shoplifters	-	-	2.5
(viii)	Withdraw legal aid for motoring offences	-	-	1.0
Total		9.4	14.8	21.1

Offsetting savings

1. No offsetting savings are offered against the bid for £40 million in 1985-86. All expenditure is by central government. Only option (i) involves capital.

Implications

(A) Court Buildings

2. The above savings could be achieved administratively but would have a knock-on effect on the construction programme.

(B) Court Services

3. The proposed reduction in jury numbers and the abolition of peremptory challenges and standing-by are policy matters for the Home Office. Both involve sensitive political considerations and would require primary legislation.

(C) Legal Services

4. Most of the measures under this heading would require primary legislation which would be controversial and meet with strong resistence from the legal profession. Options (iv), (vii) and (viii) could be seen as prejudicing the ability of persons to pursue their legal rights or to be defended in certain criminal proceedings.

5. No option involves civil service manpower.

Additional note

6. Policy relating to the recovery of court costs through fees is about to be considered by Ministers. This follows an inquiry by the PAC.

19. Department of Education and Science

Options for reductions and offsetting savings £ million cash

	1983-84	1984-85	1985-86
Offsetting savings required	240	360	365
Options for reductions required	245	375	515
Total	485	735	880
Items			
(a) Student awards: reduction in grants	20	40	50
(b) Abolish school meal service with shorter school day*	140	220	230
(c) Abolish provisions for under fives*	80	130	135
(d) Further reductions in school-teacher numbers*	40	85	130
(e) Reductions in NAFE lecturer numbers*	35	60	70
(f) Charges for primary and secondary education*	170	200	265
Total	485	735	880

*legislation required (not in 1982-83 legislation programme). Additional savings to meet the unquantified first bid would be met through increased charges under option (f).

(a) Student awards: reduction in grant

1. This option would encourage students to study near home by progressively reducing by half the differential between the grant for those living at home and those choosing to study away from home. It would also eliminate claims for additional travelling costs. It would be strongly opposed as restricting opportunities for higher education and, in effect, reducing student grants still further. It would have unpredictable effects on the viability of courses and student residences. It would operate selectively to the particular disadvantage of students living in rural areas, those obliged to spend part of their course abroad and those studying subjects where provision is concentrated in a small number of institutions.

(b) Abolish school meal service with shorter school day

2. The remaining subsidy on the school meal service covers mainly the provision of free meals for pupils from families in receipt of family income supplement or supplementary benefit or for teachers and school meals staff. Local authorities spend about £75 million on mid-day supervision. This option requires removal of the power to provide school meals and restriction of the school day in line with some continental practice (say 8 am to 1.30 pm) to avoid the cost of mid-day supervision and to weaken the case for including in supplementary benefit or family income supplement an allowance for the cost of lunch now provided free on 190 days a year. There would be much opposition from working mothers, single parents and organisations concerned with families on low incomes and the required legislation would be widely opposed as discriminating both against women generally, and against the poorest members of society. This option calls for such major adjustments in how families (as well as teachers) spend their day during term-time, as to cause much transitional disruption, and perhaps increases in crime and vandalism by unsupervised children. Even if additional resources were made available to provide facilities for 'latch-key' children, it is the DES view that the educational effectiveness of the schools would be reduced. In order to meet the requirements of the survey, it would be necessary for the new arrangements to be implemented in September 1983 hence requiring a tight time-table for the passage of highly controversial legislation.

(c) Abolish provision for under fives

3. This option would remove the power of local authorities to provide for children under statutory school age. Nursery classes and schools would close and there would be no 'rising fives' in reception classes in primary schools. There would be serious educational effects on children with difficult home backgrounds or learning difficulties arising from some other cause, for whom nursery education is a means of helping them to profit from primary and secondary education. There would again be strong opposition to such a measure from working mothers and womens' organisations. The required legislation would be highly controversial.

(d) Further reductions in school-teacher numbers

4. This would require cuts below the Cmnd 8494 planned levels in the numbers of school-teachers employed by local authorities of 7,000 in 1983-84, 10,000 in 1984-85 and 11,000 in 1985-86. As noted in paragraph 6 of the main text, Cmnd 8494 plans already require the loss of 40,000 teaching posts between 1982 and 1985. This further cut could only be secured by drastic reduction in intakes to teaching. If teacher numbers fell by 9,000 again this year, the cut would imply a virtual moratorium on recruitment in 1983, the replacement of about half the teachers leaving in 1984 and three-quarters of those leaving in 1985. Retrenchment of this order would have severe effects on the curriculum in schools and on the morale of teachers in training. To ensure that the teacher cuts were carried through, legislation to enable the Government to control the numbers of teachers employed by individual local education authorities and to qualify their obligation to provide education suitable to age, ability and aptitude would be needed.

(e) Reduction in NAFE lecturer numbers

5. This option envisages the loss of a total of 7,000 lecturer posts in non-advanced further education between 1982-83 and 1985-86. Provision in 1982-83 has been made in the light of increasing demand for places on courses from 16-19 year olds, including those on the Youth Training Scheme; a reduction in lecturer numbers of the order proposed in this option would rule out a contribution by the maintained education service to the Scheme.

(f) Charges for primary and secondary education

6. This option provides for termly charges of £10-15 in primary and secondary schools from September 1983. Parents in receipt of family income supplement or supplementary benefit would be exempt from charges (but this would worsen the poverty trap). The charges would in effect be a tax on education and the required legislation would be widely opposed as a major breach in the principle of free school education in the 1944 Education Act (and earlier Acts in respect of elementary education). A higher level of charges would lead to a pro-rata increase in the savings.

20. Office of Arts and Libraries

Options for reductions and offsetting savings

£ million cash

	1983-84	1984-85	1985-86
Offsetting savings required	72.0	95.0	110.0
Options for reductions required	11.1	17.4	24.1
Total	83.1	112.4	134.1

Offsetting savings

2. Cmnd 8494 provision implies, among other things, the withdrawal of Arts Council support for major national organisations and regional activities, less conservation work by, and public access to, the national museums and galleries, the sale of works of art abroad as the National Heritage Memorial Fund, the acceptance in lieu of tax provision and the national institutions' purchase grants are unable to cope with the growing number of private collections likely to become available for disposal, irreversible deterioration of the National Film Archive and inability on the part of the British Library to meet demands for loan stock and new information technology developments. Maintenance and capital development of the national institutions' premises will be further curtailed, with consequent implications for the preservation of historic buildings and for public access to the collections. In addition, local authority provision for public libraries and museums will also be under severe pressure, leading to restricted public access and reduced acquisition and conservation, so that growing public demand from educational, business and other users will increasingly cease to be met.

3. The flexibility which OAL has to deploy resources within the programme has permitted the pattern of activity supported to be adjusted year by year, with the result that the programme already reflects current priorities. The additional bids are therefore, by definition, for activities which are of marginally lower urgency and/or importance than those now in the programme. It would therefore be self-defeating to list specific offsetting savings to enable them to be accommodated. Offsetting savings

could be achieved only by forgoing the additional bids themselves. There is no significant scope for economy through rationalisation or elimination of waste, without affecting the level, range and quality of service.

Options for reductions

4. Given the major discrepancy already existing between planned and actual expenditure on the relevant local authority services, it would not be realistic to propose further savings on these services. Reductions of the order specified would, therefore, require to be carried entirely on the central programme. Since the central programme accounts for only about 40 per cent of the total, it follows that the percentage reductions requested for exemplification would amount to reductions in the central programme of the order of 5 per cent in 1983-84, 7 per cent in 1984-85 and 10 per cent in 1985-86. A 2 per cent reduction in the Cmnd 8494 baseline for 1983-84 would amount to some £11 million, 3 per cent in 1984-85 would be £17 million and 4 per cent in 1985-86 would be £24 million. There are two ways in which reductions of this order could be secured. First by the elimination of major central government activities (eg cessation of provision for the National Heritage Memorial Fund, purchase grants for the national museums and galleries in England and the British Film Institute - which would have to be put into liquidation) and swingeing cuts in the Arts Council grant resulting in withdrawal of support for two major national institutions (probably the Royal Shakespeare Company and English National Opera). Secondly by spreading the cuts and their affects as widely as possible over the whole programme, with consequential widespread disruption of activities. The OAL consider that the former is not politically feasible. Accordingly, reductions would be taken across the board.

21. DHSS - Health and Personal Social Services

Options for reductions and offsetting savings £ million cash

	1983-84	1984-85	1985-86
A. HOSPITAL AND COMMUNITY HEALTH SERVICES			
Offsetting savings			
None possible	-	-	-
Excess of bids over savings	301.5	430	562
Met by abandoned bids	301.5	430	562
Options for reductions			
Adjusted baseline			
current	8632	9065	9428
capital	689	724	753
Options for reductions (2/3/4%)			
current	173	272	377
capital	14	22	30
Achieved by reductions in standards			
current	173	272	377
capital	14	22	30
B. CENTRALLY FINANCED SERVICES			
Offsetting savings			
None possible	-	-	-
Excess of bids over savings	26	29	30.5
Met by abandoned bids	26	29	30.5
Options for reductions			
Adjusted baseline			
current	473	500	520
capital	27	20	21
Options for reductions (2/3/4%)			
current	9	15	21
capital	½	½	1
Achieved by reductions in standards			
current	9	15	21
capital	½	½	1

C. FAMILY PRACTITIONER SERVICES

Offsetting savings			
None possible	-	-	-
Excess of bids over savings	69½	73½	136½
Met by abandoned service bids and increased income from charges (1983-84 20% rising to 33% in 1985-86)	4	4	4
	65½	69½	132½
Options for reductions			
Adjusted baseline			
current	2586	2758	2869
capital	2	2	2
Options for reductions (2/3/4%)			
current	52	83	115
capital	-	-	-
Met by increased income from charges (1983-84 15%, 1984-85 22%, 1985-86 30%)	52	83	115
OR Half price prescription charges for exempt groups	-	50	52
OR Cost-related prescription charges	-	40	42
OR Withdrawal of general optical service	-	-	35
OR Withdrawal of general dental service	-	-	110

D. PERSONAL SOCIAL SERVICES

Offsetting savings			
None possible	-	-	-
Excess of bids over savings	207	229	259
Met by withdrawal of bids	207	229	259
Options for reductions			
Adjusted baseline			
current	1963	2072	2155
capital	110	116	120
Options for reductions (2/3/4%)			
current	39	62	86
capital	2	4	5

HCHS and CFS

(a) Offsetting savings

1. The additional cash bids in the survey report are designed to maintain the general levels of services implied in the cash provisions of Cmnd 8494 against erosion by inflation. If the bids are not granted but the higher costs nevertheless incurred, there would be serious cuts in these services.

2. The service bids are necessary, because authorities could not in general be expected to reduce present essential services to meet new pressures.

3. As explained in the survey report, DHSS believe that it is unrealistic to plan on the assumption that health authorities could make efficiency gains over and above those of about 2 per cent of their spending on hospitals and community health services between 1981-82 and 1984-85 that are already assumed in Cmnd 8494. They may, however, be able to make further efficiency savings of 0.5 per cent in 1985-86.

4. If no resources beyond Cmnd 8494 were available, we should therefore have to withdraw the service development bids. We would withdraw first the £50 million a year bid for HCHS capital. After that we would withdraw selectively and as necessary some of the service improvement bids - minimum maternity standards, hepatitis vaccination, special hospital capital, help with housing association hostels, scheme for volunteering by the unemployed, extra for district nurses and health visitors and long-stay hospital standards.

5. We should be most reluctant to withdraw bids for increased joint finance, whooping cough and rubella vaccination, help to drug misusers, demonstration projects to help the elderly severely mentally infirm, improvements for mentally handicapped children, intermediate treatment, and day-care for the under-fives; and the bids to cover demography, medical advances, and the relative price effect on purchases. The allowance for general inflation will no doubt be decided by Ministers for the public sector as a whole.

(b) Options for reductions

6. Reductions of 2-4 per cent could only come from cuts in services. The consequences for HCHS would be a widening of the gap between provision and need in services for old people, a drop in standards of long-stay care whose improvement has always been a high priority, halt to geographical redistribution, severe increases in waiting lists and waiting times and no further medical advances. Cuts in current expenditure would force authorities to leave unopened a larger number of new capital facilities than at present. By 1985-86, the number of cases treated would fall short of present standards (allowing for demographic trends) by some 180,000 and long-stay staff/patient ratios per bed would fall.

7. Cuts in health authority capital, though immediately less serious than current cuts, would reduce still further an already modest capital programme and seriously delay the replacement, renovation and maintenance of an ageing capital stock.

8. In the CFS, a significant proportion of expenditure (e.g welfare food and equipment for disabled people) is demand determined. Cuts here could not be imposed without changing the nature of the services, in some instances requiring legislation. Cuts elsewhere would mean either a reduction in standards or a complete withdrawal of essential services. These would often result in increased demands on other public services.

FPS

9. Withdrawal of the cash bid or the bid to cover increased demand would result in cash provision for the FPS being exceeded.

10. An alternative would be to increase charge income. New charges however would be inconsistent with Ministerial pledges and were ruled out in the last survey. Increases in existing charges would need to be significantly above inflation, would add to the RPI and, following substantial recent increases (eg since 1978-79 prescription charge by 290 per cent and maximum dental charge by 80 per cent, both in real terms)

would be difficult for Ministers to defend. For example, charge income would need to be increased by about 20 per cent in 1983-84 rising to 33 per cent in 1985-86 to offset in full the cost of the additional bids; and by a further 15 per cent in 1983-84 rising to 30 per cent in 1985-86 to meet the option targets. It would be necessary to raise the actual charges by rather more than these percentages.

11. Other charging options would be to:

- introduce half-price prescription and other charges for most groups now wholly exempt from charges
- relate prescription charges to cost, in place of the present flat rate
- withdraw the General Ophthalmic Services (GOS) and/or the General Dental Service (GDS).

12. Half-price charges might raise about £50 million a year from 1983-84, but would hit the groups affected - in particular the elderly and children - undermine the defence used in earlier years for increasing charges, namely that exempt groups would be protected, and break a Ministerial pledge.

13. A cost-related scheme designed to produce about £40 million a year would mean a maximum charge perhaps three times higher than the existing prescription charge. It would be administratively complex and would require legislation. It could not be introduced on a full year basis before 1984-85.

14. Withdrawal of the GOS might yield net savings of £35 million. For the GDS, the net saving might be £110 million. Withdrawal of either would require primary legislation (for which no suitable Bill is in prospect), could not be done before 1985-86, and would represent a severe weakening in the concept of the NHS.

15. Withdrawal of the GOS and/or the GDS would be the most unacceptable of these options. Cost-related presciption charges would be the next most unacceptable, followed by half-price charges and then a general increase in charges within the present arrangements. But none of the options could be adopted without the most serious political difficulty.

NHS manpower

16. The table below shows in column A (repeated from PESC Report) expected growth in NHS manpower if the planned level of expenditure in Cmnd 8494 is achieved. Column B shows the reduction in manpower which would be necessary if the full options for reductions are exercised. FPS manpower would not be affected unless the GDS were withdrawn.

Thousands

	A			B		
	1983-84	1984-85	1985-86	1983-84	1984-85	1985-86
HCHS	836	838	838	17	25	34
CFS	11	11	11	0.2	0.3	0.4
FPS	39	40	40	-	-	-
Total	886	889	889	17.2	25.3	34.4

PSS

17. The provision for local authority personal social services is indicative, and the delivery of reductions could not be guaranteed. The indicative provision for 1983-84 already implies a reduction of 3 per cent in real terms, even though social services' spending is under heavy pressure particularly because of the increasing number of very old people and growing needs in the child care field.

PSS manpower

18. The table below shows in column A the estimated local authority personal social services manpower and in column B the reductions which would have to be made if expenditure were reduced by 2 per cent, 3 per cent and 4 per cent.

Thousands

		A			B	
1981-82	1983-84	1984-85	1985-86	1983-84	1984-85	1985-86
203	198	199	199	4	6	8

DHSS manpower

19. There would be no reduction in DHSS manpower in the special hospitals, artificial limb and appliance centres and youth treatment centres arising from the options for reductions discussed above. Implications for the rest of the Department's manpower are discussed in chapter 22.

22. DHSS - Social Security

Options for reductions and offsetting savings £ million cash

	1983-84	1984-85	1985-86
Offsetting savings required*	794	1,188	1,578
Options for reductions required	234	794	1,191
Total	1,028	1,982	2,769

Illustrative savings - ready reckoner

	Part year 1983-84	1984-85	1985-86
(a) Deferring uprating for one week for each one per cent uprating	5	5	5
(b) Uprating by 1 per cent less than the movement in prices.			
"pledged" benefits (ie retirement pensions and other related long-term benefits)	60	175	180
"unpledged" benefits (ie other benefits including child benefit, supplementary allowance, sickness and unemployment benefits)	35	95	100
Total for all benefits	95	270	280

* Additional bids net of reduced requirements

1. During 1979, 1980 and 1981 various measures were taken to reduce social security expenditure as a result of which savings of about £1.5 billion have been made, mostly recurring annual savings. A wide range of possible sources of savings were considered and a number rejected as unacceptable. The scope for identifying acceptable savings through the further withdrawal of benefits rights or alteration in the entitlement rules is exceedingly limited, and no new measures have been identified. If reductions in expenditure or offsetting savings are required to be found, the only remaining ways to achieve significant savings would involve uprating benefits by less than the forecast increase in prices or deferring the annual uprating date.

2. Deferral of the uprating date is estimated to save over the 19 weeks from the normal uprating date to the end of the financial year about £95 million for each 1 per cent uprating.

3. So far as reducing the uprating is concerned, the Government is pledged to maintain the value of the retirement pension and other related long-term benefits. These account for about 60 per cent of benefit expenditure so that if the pledge is to be honoured the room for manoeuvre in saving on the cost of upratings is greatly reduced.

4. While it is not considered that savings in the general uprating of benefits would be acceptable, the above table sets out, in a ready reckoner form, the savings that would be obtained from reducing, or deferring, the uprating. The figures can be used to show how offsetting savings could be obtained through these two routes. In practice, however, it is not possible to match precisely all the bids, options and savings for each year. To do so could require actual cuts in current benefit rates.

23. Civil Superannuation

Options for reductions and offsetting savings

Most of the expenditure is for the continuing payment of pensions already in payment and for new awards under the existing provisions of the pension scheme. Reductions could not be made without retrospective legislation relating to existing pensions, or accrued rights based on past service, or both. Any of these would be highly controversial. The reduction in civil service numbers precludes making savings by allowing retirements to be deferred. A change in the contribution arrangements, including the setting up of a fully contributory civil service pension scheme, is now being considered in the aftermath of the Scott Report. Such a change would produce a substantial reduction in this programme. The saving to total public expenditure, net of the consequential increase in other programmes, would be up to £150 million a year. The earliest date by which these changes could be introduced would be 1 April 1984.

24. Scotland

Agriculture is dealt with on a UK basis in the MAFF chapter.

Industry, Energy, Trade and Employment (excluding Tourism)

Options for reductions			£ million cash
	1983-84	1984-85	1985-86
Options for reductions required	3.4	5.3	7.2

As the baseline includes the special and contingent allocation of £10 million to the Highlands and Islands Development Board (HIDB) to deal with the effects of the Invergordon Smelter closure, it has been agreed with Treasury that the required reductions should be £3.3 million, £5.2 million and £7.2 million for 1983-84, 1984-85 and 1985-86 respectively.

2. The Scottish Office view is that these reductions would seriously damage the prospect for recovery in the Scottish economy. The reductions would have a disproportionate effect because selective financial assistance is demand-related and available for any project that satisfies the criteria laid down by Ministers, which means that any reductions must fall on the provision for the two development agencies. Any curtailment in the activities of the Scottish Development Agency (SDA) and the HIDB would weaken the prospects for economic recovery, especially in the HIDB area which has been particularly hard hit by major closures such as in Lochaber and Invergordon.

For illustrative purposes, the reductions would amount to:

			£ million cash
	1983-84	1984-85	1985-86
SDA	2.6	4.1	5.8
HIDB	0.7	1.1	1.4
Total	3.3	5.2	7.2

25. Wales

Agriculture

Considered on a UK basis.

Industry, Energy, Trade and Employment (excluding Tourism)

Options for reductions £ million cash

	1983-84	1984-85	1985-86
Options for reductions required	1.6	2.6	3.6

Reductions of this order would mean substantial delays on the derelict land reclamation programme and a further decrease in the level of new factory building which the Welsh Development Agency could undertake.

Block

3. No options for reductions are exemplified because the block formula will apply.

26. Northern Ireland

Options for reductions and offsetting savings

The additional bid for housing expenditure has already been agreed by Ministers to be additional expenditure, and no offsetting savings are therefore displayed. Other bids either fall within the block and will be handled accordingly, or are within the responsibility of other Ministers. This also applies to options for reductions.

29. Other Departments

Table 29 £ million cash

	1983-84	1984-85	1985-86
Suggested reductions and offsetting savings:			
Cabinet Office (excluding secret vote)	0.464	0.409	0.566
Central Office of Information	0.857	1.348	1.870
Charity Commission	0.072	0.109	0.151
Commonwealth War Graves Commission	0.180	0.283	0.391
Crown Office	0.47	0.652	0.839
Customs and Excise	11.6	15.2	19.0
Exchequer and Audit Department	-	0.547	1.381
Friendly Societies Registry	0.511	0.410	0.257
Government Actuary	0.006	0.016	0.022
House of Commons	4.491	7.2	5.65
House of Lords	0.146	0.230	0.319
HM Stationery Office	4.633	2.726	-
Inland Revenue	18.970	7.881	63.727
Land Registry	8.183	10.940	6.808
Management and Personnel Office	0.919	1.354	1.839
National Investment & Loans Office	-	-	-
National Savings Department	2.93	4.6	6.3
Northern Ireland Court Service	0.865	0.928	0.987
Ordnance Survey	0.325	0.512	0.710
Parliamentary Commissioner	-	-	-
Paymaster General's Office	0.059	0.213	1.102
Privy Council Office	0.039	0.048	0.058
Public Record Office	0.127	0.129	0.174
Public Trustee Office	0.581	-	-
Office of Fair Trading	0.101	0.159	0.220
Office of Population, Censuses & Surveys	0.124	-	0.031
HM Treasury: Administration, note issue etc	1.935	2.377	2.231
HM Treasury: Rates on Government Property Department	-	-	-
Treasury Solicitor's Office	0.318	0.519	0.718
Total	58.906	58.790	115.351

29. Other Departments

Cabinet Office (excluding secret vote)

1. To meet the options for reductions and offsetting savings the Cabinet Office would have two choices:

(i) to forego any further development of its computer facility; or

(ii) to cut back the functions of the office by abolishing either the Central Policy Review Staff or a Secretariat. There would be no need for legislation. These measures seem drastic and the Treasury wishes to explore with the Department whether any less extreme measures would be feasible.

Central Office of Information

2. Options for reductions would have to be taken on the publicity campaigns for Government Departments including major campaigns on Energy Conservation, Road Safety and Services recruitment. Overseas publicity for Foreign and Commonwealth Office which is largely in support of exports and has been severely cut back over recent years, would be further reduced.

Charity Commission

3. The option cuts would only be possible if primary legislation was introduced in order to reduce the Commissioners' statutory functions.

Commonwealth War Graves Commission

4. The UK Government's contribution to the Commission provides for the major part of the Commission's expenditure and is fixed at 78 per cent. The remainder is provided for by contributions from five other Participating Governments and in order to reduce the Commission's expenditure it is necessary to secure the agreement of these other Participating Governments. Substantial savings could be achieved only by a reduction in staff costs, which represent over 80 per cent of total expenditure. The options for reductions imply staff reductions in the range of 25 - 50 posts in addition to those already planned for 1982-83 and later years.

Crown Office

5. Options for reductions and offsetting savings could only be achieved by:

(i) a further increase in the fixed penalty for parking offences from the present level of £10. The Secretary of State for Scotland's approval would be needed but the income would accrue to the Crown Office; or

(ii) a reduction in the level of prosecution in Scotland by the Crown Office which would increase the prospect of offending with impunity.

Customs and Excise

6. The required options and offsetting savings in 1983-84 could only be met by restricting or stopping recruitment leaving local management to handle the work as best they could, because all of the following options require legislation and/or consultation. This would have arbitrary and unpredictable effects on the machinery of revenue collection (eg computer operations), enforcement standards and the law and order functions of the Department.

7. The options and offsetting savings in 1984-85 and 1985-86 could be met by the following:

(1) Annual accounting with annual payment for small businesses whose annual liability does not exceed £2,000 per year (£4,000 per year if option 4 is also introduced and the total savings are to be maintained) would save an estimated £1.5 million (150 staff) each year. Revenue loss is likely to be minimal but there will be a once and for all PSBR cost of £115 million with a full year interest cost of £14 million. Subordinate legislation would be required.

(2) The abolition of duties on bingo, gaming machines and casinos (whilst retaining those on pool betting and general betting) would save about £0.9 million (90 staff) in each year. The annual revenue loss is estimated as some £105 million. Main legislation would be required in 1983.

(3) The restriction of Customs attendance at ports and airports to control traffic and clear freight only at specified hours. If these were sufficiently restrictive, it could be possible to save an estimated £6.6 million in 1984-85

and £6.9 million (600 staff) in 1985-86. Main legislation would not be required but there would need to be extensive consultation as such action would curtail and distort established trade patterns and practices. The measure would undoubtably provoke considerable opposition from port and airport authorities and other commercial interests. The alternative of universal charging for attendance outside such specified hours would reduce public expenditure but would produce staff savings only as and when operators altered their practices.

(4) Compulsory deregistration of VAT traders below the threshold in this year's Finance Bill would save an estimated £2.0 million in 1984-85 and £3.7 million (370 staff) in 1985-86. There would be an initial cost in 1983-84 because of the staff effort required to effect deregistration of large numbers of traders. An increase in the VAT yield of up to £40 million might be expected. Main legislation would be required in 1983. There would be widespread and very considerable opposition. The action would be seen as a blow to small traders and particularly unfair to those enjoying a net repayment of VAT. A minimum registration limit could be held to be in breach of the EC 6th Directive.

(5) Compulsory deregistration of VAT traders below a raised threshold of £24,000 would save an estimated £4.2 million in 1984-85 and £6.1 million (600 staff) in 1985-86 (additional to option 4). It is estimated that there would be a revenue loss of around £140 million a year. Main legislation would be required in 1983. The opposition would be greater than for option 4 and the measure would be in breach of the EC 6th directive.

Exchequer and Audit Department

8. Options for reductions in 1983-84 would be met by a reduced requirement. The remaining options and offsetting savings, which would fall on manpower, could only be achieved by reducing the scope and quality of the audit.

Friendly Societies Registry

9. Options for reductions and offsetting savings could only be achieved by reducing the staff complement of the Department. This would require the temporary suspension

of certain functions and the abolition of others, thereby impairing the supervisory role of the Department. In 1985-86 further savings could be achieved by an increase in charges for building society work. Legislation would be required to produce most of these savings.

Government Actuary

10. The Department's expenditure is exclusively on staff and general administrative expenditure. The reductions shown are equivalent to one Assistant Actuary fewer in 1983-84 rising to one Actuary and one Assistant Actuary fewer in 1985-86. Cuts would seriously impair the capacity to provide actuarial advice in major areas of government.

House of Commons

11. No options or offsetting savings have been supplied by the House of Commons on expenditure which they control. The House Authorities point out that expenditure on salaries and allowances for MPs is demand led. Any reductions would have to come from reductions in staffing and related expenditure by the House of Commons Commission. The House of Commons Commission have not identified any options or offsetting savings. These would require a reduction in staff and in the level of service which the Commission provides to MPs and therefore the agreement of the House of Commons. The reductions shown have been calculated by Treasury divisions and are illustrative only.

House of Lords

12. Owing to the nature of Parliamentary expenditure no options for reductions can be forecast. To achieve any reductions it would be necessary to consider with the House Authorities the possibility of reducing services to the House of Lords with resulting savings in staff costs and related expenditure. The options shown are therefore illustrative only.

HM Stationery Office

13. Options for reductions in 1985-86 have been met from a reduced requirement. Options for reductions in 1983-84 and 1984-85 might be met from reductions in the amount which HMSO are permitted to borrow. This would be likely to result in either the cancellation or deferment of capital projects with a consequent adverse effect on

the performance of the Trading Fund. The alternatives are to increase further the price of Hansard or reverse the decision to maintain the present level of discount in the sale of government publications to public libraries. HMSO has no power to enforce a reduction in the provision for supplies to Parliament.

Inland Revenue

14. Offsetting savings for the additional bids for 1983-84 and 1985-86 and options for reductions would require further staff reductions which in turn might require legislative or fiscal changes of a budgetary nature affecting the numbers of taxpayers of various kinds.

15. Such changes could include, increases in tax thresholds which, although saving staff, would involve a considerable loss of revenue. The following table shows the relationship between staff savings and revenue costs of threshold adjustments:-

Increases in tax thresholds (per cent)	Cost of staff saved £ million	Revenue lost £ million
10	7	1,830
20	12	3,470
30	18	5,060
40	23	6,590

Land Registry

16. Options for reductions and offsetting savings imply reduced gross expenditure of £8.183 million in 1983-84, £10.940 million in 1984-85 and £6.808 million in 1985-86. Public demand for land registrations would not be met and receipts, which on present plans will substantially exceed gross expenditure throughout the survey period, would suffer.

Management and Personnel Office

17. To meet the options for reductions and offsetting savings the Management and Personnel Office would need to:

(i) curtail recruitment by the Civil Service Commission for certain classes or grades which would require an amending Order on Council to adjust the statutory responsibilities of the Commissioners; and

(ii) in addition a severe pruning of the Management studies and Policy and Administrative Directorate in the Civil Service College would be required, with perhaps an amalgamation of the two options.

National Investment and Loans Office

18. Net expenditure on this programme is a token £1,000 a year because NILO generates sufficient receipts to cover its original costs, and therefore percentage options are nil.

National Savings Department

19. Reductions at the lower end of the scale of options would be made by:

(i) pruning advertising: a step which could damage DNS's position in the highly competitive savings market and hence its funding role.

(ii) The higher options for 1984-85 and 1985-86 would in addition require a policy change designed to reduce the number of transactions handled deliberately restricting sales of savings certificates to aim mainly at those investors with larger sums to invest. To attract large investors the Department would need to offer significantly better returns than those offered by competitors. For any given borrowing targets the effect of these options would be to increase the cost of the interest/tax concessions on the new borrowing.

Northern Ireland Court Service

20. Options for reductions and offsetting savings would be met by:

(i) postponing the new court building programme; and

(ii) raising the recovery rate on court fees.

Ordnance Survey

21. It is expected that the Ordnance Survey will become a Trading Fund on 1 April 1983. In that event, the survey's net borrowing from the National Loans Fund will be the only expenditure attributable to the Ordnance Survey programme. However, there will in addition be a contract payment to the Survey from the Department of the

Environment which will count as public expenditure. The options for reductions will then need to be considered.

Parliamentary Commissioner

22. Options for reductions have been met from reduced requirements.

Paymaster General's Office

23. Reduced requirements in 1983-84 and 1984-85 go some way towards the options for reductions. As the level of demand for the Departments service is outside its control, the balance of the options and the offsetting savings would only be achieved by:

(i) abolishing the Analysis of Public Expenditure (APEX) monitoring system. This would save £200,000 a year but would deprive the Treasury of important financial monitoring information; or

(ii) of abandoning the weekly payment of certain pensions which would save up to £2.1 million a year. This would require the agreement of the Unions and would undoubtedly be vigorously opposed.

Privy Council Office

24. Options for reductions and offsetting savings could only be achieved by reducing the staff of the Department and replacing an Assistant Secretary presently on detached duty. This would however impair the effective functioning of the Department and would require the agreement of the respective Ministers.

Public Record Office

25. Options for reductions and offsetting savings for the installation of a machine readable records system and storage of Government film records would be achieved only by:

(i) reductions in the general level of services provided to the public; or

(ii) the introduction of charges for inspecting the records; or

(iii) a reduction in conservation work; or

(iv) a combination of these measures.

Charges were rejected in the Government's recent response to the Wilson Committee Report on Modern Public Records. Reduced conservation could put historic documents at risk. Staff reductions would be contrary to a recent assurance given in the House. A further additional bid totalling £2 million of the survey for essential repair work at Chancery Lane is too large in relation to the existing programme to be offset.

Public Trustee

26. Offsetting savings will be financed from receipts received from fees and charges.

Office of Fair Trading

27. Options for reductions would be from cutback in codes of practices work under the Fair Trading Act.

Office of Population Censuses and Surveys

28. The options for reductions would be met partly from reduced requirements. In 1983-84 and 1985-86 the balance of the options would require the discontinuation of certain surveys and statistical operations. No legislation would be required.

HM Treasury; Administration

29. Around two-thirds of the expenditure is staff related and before putting forward the additional bids (which are net figures), full account has been taken of the various measures to reduce the cost of administration. Offsetting savings in 1983-84 and 1984-85 could only be achieved by cuts in computer and telecommunications fee paid services and development studies. Such reductions would prejudice the ability of the Central Computer and Telecommunications Agency to obtain value for money in computers and telecommunications expenditure and delay the development and application of new technology. The Treasury does not consider this feasible. Any significant reductions in the baseline figures could only be attained by reducing the Treasury's capacity to handle and advise on the financial and economic issues which come before Government.

HM Treasury: Miscellaneous

30. The House authorities have been unable to identify any offset to additional bids for computer services to the Houses of Parliament and so no offsetting savings are shown. Additional bids in 1981-82 and 1982-83 were offset by savings in Central Computer and Teleommunications Agency Services but this is no longer practicable since any savings which the Agency find are required to offset its own additional bids mentioned in the previous paragraph. Offsetting savings for payment of pensions and lump sums to United Kingdom Members of the European Assembly who retire or are not re-elected in June 1984 are not available as once again this is Parliamentary expenditure. Finally offsetting savings are shown for a bid to increase the communications work of the tripartite committees of the National Economic Development Council. But these would require a reduction of 3-4 per cent in the existing staff of NEDC and would impair its activity to an unacceptable extent.

31. Further reductions to meet the options for reductions are not practicable. Almost 70 per cent of expenditure under this heading is made from the Consolidated Fund and is demand related. In some cases reductions would require legislation. Wherever the balance of expenditure is within the direct control of the Treasury, full account has been taken of Ministerial targets for manpower reductions and associated expenditure.

HM Treasury: Note issue, debt management and coinage

32. All the services provided by the Bank of England reflect Government monetary and debt management policy and the level of activity necessary to implement such policy. Any reductions would be dependent on what would be major changes in the underlying policy. Briefly, there are no possibilities for reducing expenditure on the Exchange Equalisation Account, any further reduction in staff numbers engaged on British Government stocks management would be likely to lead to an unthinkable failure of operations in the gilts market. The note issue is demand determined and the expenditure on Note Issue is miniscule in comparison with the Profits of the Issue Department which is directly related to the face value of notes issued. The quality of the Note Issue has already been reduced and has been subject of criticism, any further reduction would be controversial and potentially dangerous.

33. Expenditure on coinage is demand led and no reductions can be made unless Ministers change their view that demand for coins should be met in full. In addition, the production of coins produces a profit for the Exchequer.

HM Treasury: Rates on Government Property Department

34. Rate payments are the only expenditure in this programme. Administrative costs are included in the figure for HM Treasury (Administration). The department does not determine the amount of Government property occupied and cannot, therefore, offer realistic or achievable options for reductions.

Treasury Solicitors Department

35. There are no feasible offsetting savings in 1983-84. Some offsetting savings in manpower will become available in later years if the computer facilities are installed. It is proposed to cover the options for reductions by a functional change following which the cost of conveyancing will be charged to user Departments on a repayment basis. (Initial discussions have already started on this charge.) The options for reductions would be to withold some of the existing provision (£2.2 million, £2.3 million, £2.4 million) when the conveyancing work was transferred to a repayment basis.

ANNEX A

Options for reductions and offsetting savings 1983-84 - 1985-86

Options for reductions and offsetting savings by Department and broad economic category

£ million cash

Capital/ Current		1983-84	1984-85	1985-86
	Ministry of Defence			
	Foreign and Commonwealth Office - Overseas Development Administration			
CUR	Net aid programme	20.3	32.0	44.4
CAP	CDC	0.3	0.4	0.6
CUR	Overseas aid administration	0.5	0.7	1.0
	Total	21.1	33.1	46.0
	Foreign and Commonwealth Office - Other			
CUR	Overseas representation	9.4	14.1	19.5
CUR	Overseas information	-	0.5	1.0
CUR	Other external relations	0.5	0.7	0.7
CUR	Military aid	0.3	0.4	0.5
	Total	10.2	15.7	21.7
	European Community			
	Intervention Board for Agricultural Produce			

£ million cash

Capital/ Current		1983-84	1984-85	1985-86
	Ministry of Agriculture, Fisheries and Food			
	Agriculture, Fisheries and Food			
CUR	Estimating reductions	8.4	10.2	21.8
CUR	Deferment of agreed AHDS target income option	1.2	2.0	2.1
CAP	Land sales	-	1.2	-
CAP	Reductions in capital grants	17.0	25.0	35.0
CAP	Thames tidal defences	-	-	5.2
	Total	26.6	38.4	64.1
	Forestry Commission			
CAP	Timber receipts	-	-	1.2
CAP	Reduction in vehicles, etc	0.9	0.4	1.6
CAP	Capital building work	-	0.2	-
CAP	Materials, services and administration expenses	0.4	1.3	0.7
	Total	1.3	1.9	3.5
	Department of Industry			
CAP		24.0	30.0	43.0
	Department of Energy			
CUR	Nuclear R & D	9.4	15.2	21.5
CUR	Non-nuclear R & D	0.5	1.0	1.0
CUR	Energy conservation	0.4	0.6	0.8
CUR	Departmental administration	0.2	0.2	0.2
	Total	10.5	17.0	23.5
	Department of Trade			
	Elimination of ECTMO provision	-	2.6	2.6
CUR	Withdrawal of bids	3.0	3.4	10.9
	Total	3.0	6.0	13.5

Capital/ Current		£ million cash 1983-84	1984-85	1985-86
	ECGD			
CUR	Raising of fixed rates under the consensus	28.8	35.6	43.4
CUR	Yen facility	3.7	4.5	5.6
CAP	Refinance	50.0	-	-
CUR	Withdrawal of matching facility	5.4	5.7	5.9
	Total	87.9	45.8	54.9
	Department of Employment			
CUR	Reductions within the MSC	29.4	49.4	6.7
CUR	Reductions within the HSC	1.8	2.8	-
CUR	Reductions in the Community Enterprise Programme	2.2	-	-
	Reductions in rebate to employers from the redundancy fund:			
CUR	- from 41 to 36 per cent	-	24.5	-
CUR	- from 46 to 29 per cent	-	34.5	-
	Total	33.4	111.2	6.7
	Department of Transport			
	Capital spending			
CAP	Motorway/trunk road construction	33.0	44.0	59.0
CAP	Local transport	36.0	49.0	64.0
	Central government subsidies to transport industries:			
CUR	British Rail	39.0	58.0	79.0
CUR	Other	1.0	2.0	3.0
CUR	Ports	7.0	6.0	7.0
	Miscellaneous:			
CUR	Driver and Vehicle Licensing Centre	3.0	4.0	5.0
CUR	Other transport services	2.0	3.0	5.0
	Total	121.0	166.0	217.0

Capital/ Current		£ million cash 1983-84	1984-85	1985-86
	Department of the Environment - Housing			
CUR		1035.0	911.0	749.0
	Department of the Environment - PSA			
CAP	Operational requirements (6 schemes)	1.0	1.8	2.3
CUR	Lease expiry (2 schemes)	2.3	3.4	1.6
CAP	Overcrowding/increased efficiency	1.5	3.8	4.1
	Total	4.8	9.0	8.0
	Home Office			
CUR	Police superannuation	32.4	-	-
CUR	Prisons	15.8	21.6	15.7
CUR	Police civilians	2.0	1.1	-
CUR	Fire (cg)	1.3	1.4	-
CAP	Civil defence (la)	3.6	4.1	4.1
CAP	Local authority capital	10.0	10.0	10.0
	Total	65.1	38.2	29.8
	Lord Chancellor's Department			
CAP	Court Buildings:			
	Postponement of site acquisition and construction starts on new buildings	0.6	1.2	3.0
	Court Services:			
CUR	Reductions of jury from 12 to 10	2.3	2.3	2.3
CUR	Juries: abolition of peremptory challenges and standing-by	-	1.0	1.0
	Legal Services:			
CUR	Restrict advice and assistance to matrimonial and criminal matters	6.5	7.5	8.5

£ million cash

Capital/ Current		1983-84	1984-85	1985-86
CUR	Rights of audience for prosecuting solicitors in the Crown Courts	-	0.8	0.8
CUR	Separate but fair remuneration for matrimonial legal aid	-	2.0	2.0
CUR	Withdraw criminal legal aid for shoplifters	-	-	2.5
CUR	Withdraw legal aid for motoring offences	-	-	1.0
	Total	9.4	14.8	21.1
	Department of Education and Science			
CUR	Student awards: reductions in grants	20.0	40.0	50.0
CUR	Abolish school meal service with shorter school day	140.0	220.0	230.0
CUR	Abolish provision for under-fives	80.0	130.0	135.0
CUR	Further reductions in schoolteacher members	40.0	85.0	130.0
CUR	Reductions in NAFE lecturer numbers	35.0	60.0	70.0
CUR	Charges for primary and secondary education	170.0	200.0	265.0
		485.0	735.0	880.0
	Office of Arts and Libraries			
CUR	Withdrawal of additional bids	72.0	95.0	110.0
CUR	Across the board cuts	11.1	17.4	24.1
		83.1	112.4	134.1
	DHSS - Health and Personal Social Services			
CAP/CUR	Hospital and Community Health Services: Withdrawal of bids	301.5	430.0	562.0
CUR	Reductions in standards - current	173.0	272.0	377.0
CAP	capital	14.0	22.0	30.0

£ million cash

Capital/ Current		1983-84	1984-85	1985-86
	Centrally Financed Services			
CAP/CUR	Withdrawal of bids	26.0	29.0	30.5
CUR	Reductions in standards - current	9.0	15.0	21.0
CAP	capital	0.5	0.5	1.0
	Family Practitioner Services			
CAP/CUR	Withdrawal of bids	4.0	4.0	4.0
CUR	Increased charges (1983-84 20% rising to 33% in 1985-86)	65.5	69.5	132.5
CUR	Increased charges (1983-84 15%, 1984-85 22%, 1985-86 30%)	52.0	83.0	115.0
	or half price prescription charges for exempt groups	-	50.0	52.0
	or cost related prescription charges	-	40.0	42.0
	or withdrawal of general optical services	-	-	35.0
	withdrawal of general dental services	-	-	110.0
	Personal Social Services			
CUR	Withdrawal of bids	207.0	229.0	259.0
	Total*	852.5	1154.0	1532.0

*Includes increased charges for Family Practitioner Services of £52 million, £83 million and £115 million respectively in 1983-84, 1984-85, 1985-86 but excludes the alternatives also shown in the table.

£ million cash

Capital/ Current		1983-84	1984-85	1985-86
	DHSS - Social Security			
	Offsetting savings	794.0	1188.0	1578.0
	Options	234.0	794.0	1191.0
	by (a) deferring uprating for each one week per cent uprating			
	(b) uprating by 1 per cent less than the movement in prices "pledged" benefits (ie retirement pensions and other related long-term benefits) and "unpledged" benefits			
CUR	Total	1028.0	1982.0	2769.0
	Civil Superannuation			
	Scotland			
CAP	SDA	2.6	4.1	5.8
CAP	HIDB	0.7	1.1	1.4
		3.3	5.2	7.2
	Wales			
CAP		1.6	2.6	3.6

	£ million cash		
	1983-84	1984-85	1985-86
Capital/ Current			
Northern Ireland			
Other Departments			
CAP/CUR	58.9	58.8	115.4

10 DOWNING STREET

(1)

Prime Minister

The Chancellor wonders if Terry Burns could again come to the economic / public expenditure Cabinet tomorrow.

Agree? Yes MT

MCS 14/7

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cc Mr. Mount
Mr. Vereker

MR. SCHOLAR

THE OUTLOOK FOR INDUSTRY: THE JENKINS PACKAGE

1. The leading indicators are good. The leading indicators have an excellent record - they forecast the pause in recovery and now they forecast the continuation of the recovery. If the indicators were forecasting a decline, then there may well be a case for considering some sort of package. But they are not. And the most sensitive of the indicators, housing starts, is showing a dramatic 40% rise. on last year - but caution: there is some evidence that the upward trend is levelling out (see flag A). MCS

2. This would be interpreted as a mini-Budget and would cause concern if not crisis in financial markets. It would be widely seen as a Government U-turn, a pre-election bonanza, just like all other previous governments have indulged in. Such increases in spending would be represented as the height of folly just after we have had all the expenses of the Falklands conflict. From January 1981 we have avoided interim budgets by introducing a consistency and stability in our budgetary and financial system - and this is much admired both by the City and by foreigners. Confidence has been hard to gain; it is, alas, easy to lose.

3. It would increase interest rates. Markets would rapidly revise their expectations of future inflation rates in the UK and interest rates would adjust upwards. Even quite modest increases in the borrowing requirement would be interpreted, as they are in America, as harbingers of larger deficits to come. Protestations that we were still sticking to our MTFS would be greeted with scepticism or derision. As we saw in March 1981, the only thing that will convince markets are actions. One might well fear that we would drift into a situation similar to the disastrous financial conditions that obtain at present in the United States; high budget deficits, high interest rates and no confidence in the Government's fiscal and financial policy. Recent experience in OECD countries shows that the budget deficit has an amplified effect on interest rates which would more than negate any supposed expansionary effect of an increased deficit. So we should do nothing to jeopardise the progressive fall in interest rates which is the best way to emerge from the slump.

/4. Hire Purchase Controls

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4. Hire Purchase Controls

Of all the recommendations which are made in the letter, the one we should accept immediately without reservation is to abolish hire purchase controls. This has been discussed between the Chancellor and the Governor and there is agreement on this issue. The Chancellor's letter to Lord Cockfield of 13 July refers.

attached

MCS

14 July 1982

ALAN WALTERS

Ref: A09015

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PRIME MINISTER

Public Expenditure and Economic Prospects
(C(82) 27 and 28)

BACKGROUND

This is the first substantive discussion by Ministers collectively of the 1982 Public Expenditure Survey. Of the two memoranda on the agenda, the Chancellor of the Exchequer's paper (C(82) 27) sets the economic background; that by the Chief Secretary, Treasury (C(82) 28) is the one requiring decisions. These decisions relate to overall totals, and would provide the framework for ensuing discussions on individual programmes.

Para A

Para B

Economic Prospects

2. It has been clear, from the discussion in the Ministerial Committee on Economic Strategy and from other indications, that some Ministers, and notably the Secretary of State for Northern Ireland, may want not so much to challenge the Chancellor's judgment on economic prospects on the basis of present policies as to argue that, because economic recovery is late in coming and likely to be slow to get under way on the basis of those policies, there is an economic and political case for relaxing the strategy so as to allow a little more stimulus than is implied in the Chancellor's judgments and forecasts.

3. The Secretary of State for the Environment may well renew his argument for encouraging more investment, if necessary at the expense of some of the existing commitments on the indexing of transfer payments.

4. You will no doubt feel that you should let this discussion happen. It seems likely that the broad consensus of the Cabinet will be to the effect that the Government's financial strategy is beginning to bear fruit, and that this is no time to depart from it.

5. Moreover, if there is room for fiscal manoeuvre in the 1983 Budget, you and the Chancellor - and your colleagues - will want to have as much as possible of it available for tax reductions, which would have political as well

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as economic priority. You would not want, by relaxing the grip on public expenditure, to pre-empt or unduly to limit the possibility of easing the burden of taxation. In that sense, the discussion on economic prospects ought not to provide - at any rate at this early stage - a reason for a different judgment on public expenditure totals and objectives than those suggested in the Chief Secretary's paper.

Public Expenditure

6. The present public expenditure planning totals are £120.5 billion for 1983-84 (compared with £113.9 billion in the March 1981 White Paper); and £127.7 billion for 1984-85. The base-line for 1985-86 is £133.3 billion; but that is arrived at not on the basis of a review of individual programmes but by increasing most programme figures for 1984-85 by 4 per cent. It was estimated at the time of the last Budget that the plans would allow room for tax reductions (beyond revalorization) of £0.5 billion in 1983-84; the latest economic forecasts apparently do not greatly change the position.

7. Bids from Departments for additional expenditure total some £6 billion in 1983-84 and £7¾ billion in 1984-85 (apart from any Falklands consequentials, on which the Chief Secretary puts a provisional figure of £250 million a year). To hold the planning totals will require most of the bids to be withdrawn, or offset by savings elsewhere.

8. The Chief Secretary therefore asks that the aim should be to hold to the present planning totals for public expenditure in 1983-84 and 1984-85 and that he should hold bilateral discussions with spending Ministers, with a view to reporting back to Cabinet in October. He also proposes that the Civil Service manpower figures for 1st April 1984 in the 1982 PESC report (totalling 630,000, detailed breakdown in Table E.2 on page 185) should be treated as firm limits: that is, no Department should have a higher figure; but he would be free to propose lower figures in particular cases.

End-Year Flexibility

9. Finally, a further memorandum by the Chief Secretary, Treasury (C(82) 29), on end-year flexibility, has been circulated. You have indicated that you do not wish the substance of it to be discussed.

Page —

MAIN ISSUES

10. Ministers will be acutely aware that, however desirable it is to stick to the published public expenditure totals, that will entail some very difficult decisions. Some may question the wisdom of such decisions in the run-up to a General Election. Of the bids listed in the Annex to C(82) 28, those for the Export Credits Guarantee Department, social security and local authority current expenditure are virtually inescapable; and no doubt some of the others will have to be conceded in whole or in part. It may be reasonable to reckon on additions of about £2½ billion being unavoidable. To offset them may well require contentious measures to find savings - besides the withdrawal of all 'optional' bids.

11. Ministers may therefore ask whether these difficult choices can be avoided, for example:-

(a) by using the Contingency Reserve;

(b) by assuming more buoyant revenue (thus permitting both tax reductions and somewhat higher public expenditure)

(c) by arguing that the inflation factor for 1983-84 and thus the cash total for that year should be revised upwards;

(d) by arguing that the PSBR will again, as in 1981-82, be lower than forecast.

Brief comments on each of these points are set out below.

Use of the Contingency Reserve

12. The planning figures include contingency reserves of £4 billion in 1983-84 and £6 billion in 1984-85. The Chancellor is likely to accept that it would be reasonable at this stage to allocate some part of the Contingency Reserve for 1983-84 to individual programmes. But it would be imprudent to use the whole reserve before the start of the year: the Chancellor and the Chief Secretary will want to have an uncommitted reserve of at least £2 billion (at the start of 1982-83, the reserve was £2.4 billion). Thus if a reasonable uncommitted reserve is to be maintained, it will not cover the whole of the bids likely to be found inescapable, let alone others.

Buoyancy of the Revenue

13. Part of the reason for the bids for additional expenditure is that pay settlements have been higher than allowed for in the planning totals. It may therefore be argued that higher incomes will generate higher revenue. However, we understand that the calculations behind the Chief Secretary's memorandum already allow for this effect: it therefore does not increase the room for a positive fiscal adjustment or reduce the need to keep public expenditure within planning totals.

Inflation Factor

14. The general inflation factor used for this year in the public expenditure plans is 6 per cent. The current forecast for price inflation is around 7 per cent; and Ministers endorsed the proposals in the Chancellor of the Exchequer's recent note on the next pay round (E(82) 53) to go for an increase in public service earnings substantially below the level of the current round. There would not therefore seem to be a case at present for justifying an increase in the 1983-84 total on the grounds that the inflation factor may need to be revised.

Uncertainty of the Forecasts

15. The Chancellor recalls in paragraph 10 of C(82) 27 that the 1981-82 PSBR was £1½ billion below forecast. Some Ministers may feel that in the public expenditure discussions last autumn they agreed on the basis of gloomy PSBR forecasts to restrain expenditure more than they would have wished and that the same may happen in this round. However the Chancellor argues that analysis suggests that the 1981-82 shortfall will not be carried through into future years: there may be a small shortfall in 1982-83, but if there is any it is likely to be much less than last year. There will be an opportunity to review the position in the autumn.

Other Points

16. Other points may be raised in discussion about manpower, where the Chief Secretary is now proposing to convert the 1st April 1984 targets into firm limits, and about the Chancellor's ideas for "positive action" in paragraphs 14 to 17 of C(82) 27. In both cases any points might best be pursued separately with the Ministers concerned.

17. In this latter context there may be some discussion of the suggestions in the Secretary of State for Industry's letter of 13th July arguing for an "autumn package" of measures worth about £1 billion to industry's cash flow, including a further reduction in the National Insurance Surcharge, some specific proposals involving public expenditure and some relaxation of hire purchase controls. Treasury Ministers are likely to argue that the expenditure proposals will have to be considered in the course of the bilateral discussions in the normal way and that the time to reach decisions on these and on any further reduction in the National Insurance Surcharge is the autumn.

HANDLING

18. You will wish to open the discussion, perhaps by a brief political scene-setting, and then to invite the Chancellor of the Exchequer to speak to his paper on the economic prospects. I suggest that it would be best to let the discussion run on this general level for a time, until you are in a position to express some kind of consensus, before inviting the Chief Secretary, Treasury to introduce his proposals on public expenditure. You may want to make sure of eliciting contributions to the ensuing discussion from the "big spenders", and particularly the Secretaries of State for Defence, Education and Science, the Environment (for local government) and Social Services. The Lord Privy Seal may want to comment on the proposal that the Civil Service manpower forecasts for 1st April 1984 should now be treated as firm limits.

CONCLUSIONS

19. You will wish to reach conclusions on the following lines:

(a) In relation to the Chancellor of the Exchequer's paper, C(82) 27:

(i) Taking note of the economic assessment and broad strategy.

(ii) Developing, if appropriate in the light of the discussion, the references in paragraphs 14 to 17 of the paper to positive action relating to unemployment, enterprise and the competitiveness of industry.

(b) In relation to the Chief Secretary's paper, C(82) 28:

(i) Endorsing or otherwise the aim of holding to the present planning totals for expenditure in 1983-84 and 1984-85

(noting that this means only the minimum additions to programmes and compensating reductions in other programmes);

(ii) Adopting, subject to any points made in discussion, the Civil Service manpower totals for 1st April 1984 as firm limits.

(iii) Inviting the Chief Secretary to have bilateral discussions with spending Ministers and to report back to the Cabinet in October.

RTA

Robert Armstrong

14th July 1982

10 DOWNING STREET

From the Private Secretary

Prime Minister

Public expenditure Cabinet

(1) I attach a note by Alan Walters with arguments against the P Jenkin approach.

I also attach

(i) a Treasury letter which shows that, for good tactical reasons, the Public Expenditure figures considerably understate – by up to £250-350m a year the EC Budget contribution (flag B)

(ii) at flag C a table showing how tax has grown since 1979 as a % of GDP to well above Labour govt levels

PTO

(iii) at flag D a table showing how public expenditure as a % of GDP has similarly risen since 1979 to well above Labour Govt levels

(2) I haven't been able to get very far yet on who was behind Mr Jenkin's letter. It was, apparently, conceived several weeks ago. The Chancellor has protested to Mr Jenkin about the way in which, and the time at which, it was launched.

MCS 14/7

(3) Some Minister may make use of Sam Brittan's argument for a stimulus. A note by Terry Burns rebutting this is at flag E

1. Total taxation as a percentage of GDP at market prices

1973-74	33.4
1975-76	36.6
1978-79	34.5
1979-80	35.8
1980-81	37.4
1981-82	40.0
1982-83	39.3 estimate

Source Treasury Budget brief

Note: Real value of single and married allowances is in 1982-83, after the Budget changes, about 3% lower than in 1978-79

D

Public Expenditure as a Percentage of GDP at Market Prices

1975-76	46%
1976-77	44½%
1977-78	40½%
1978-79	41%
1979-80	41%
1980-81	43½%
1981-82	44½%
1982-83 (estimated)	44½%

Source Public Expenditure White Paper Command 8494 - 1

~~Public Expenditure Total~~ ~~1982-83 = £115b.~~

1983-84 = £121b.

1983-84
+ existing
bids for
additions
= ~~around £128b~~.

Prime Minister

B A.J.C. 14/7.

(2)

CONFIDENTIAL

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

13 July 1982

A.J. Coles, Esq.,
No.10 Downing Street

Dear John,

PUBLIC EXPENDITURE SURVEY AND NET CONTRIBUTIONS TO EUROPEAN COMMUNITY

The Chancellor has asked me to send you a note about the figures for net contributions to EC institutions which will appear in this year's survey report. These are summarised in the table below.

Net Payments to EC Institutions (excluding aid)

	£ million			
	1982-83	1983-84	1984-85	1985-86
Last White Paper/baseline (Cmnd 8494)	500	580	600	[624]
New figures	635	430	514	687
Difference	+135	-150	-86	[+63]

Underlying the new figures is a somewhat more favourable projection for our net budget contribution before refunds than implied by the last White Paper. The 1 per cent VAT ceiling is assumed to be maintained.

The main change, however, is a new assumption about UK budget refunds for 1982, based on the recent agreement. The last White Paper made the 'stylized' assumption that, following the precedent of the 30 May agreement for 1980 and 1981, we would receive each calendar year refunds equivalent to 66 per cent of our net contribution before refunds for the previous year. The new figures make the same assumption for 1983 and subsequent years but take account of the recent agreement on budget refunds for 1982, which was less favourable to the UK. This affects both the amount and the timing of our refunds. The total amount is reduced by some £120 million, and some £115 million of the net refunds which we expected to receive during the current financial year are now expected to come in during 1983-84 or 1984-85.

/The point

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The point which particularly concerns the Chancellor is the risk that the actual figures for 1983-84 and the later years could be much worse than the survey report figures. As explained above, and in the report itself, the survey figures assume that, for 1983 and later years, we shall again receive refunds equal to 66 per cent of our uncorrected net contribution, as implied by the 30 May 1980 agreement for 1980 and 1981, as against the 55½ per cent figure implied by the 25 May 1982 agreement for 1982. The figures make no allowance, moreover, for any repayments by the UK on account of the so-called 'overpayment' of refunds for 1980 and 1981. The Chancellor hopes that the outcome will indeed be as favourable as this, or more so, but feels that we can by no means count on it. The others may well try, for example, to impose on us a deal which -

(a) gives us a basic refunds percentage of around 55 per cent, as for 1982, and

(b) obliges us to repay (say) £300-4oo million over a period of (say) two or three years on account of the so-called 'overpayment' for 1980 and 1981.

The Chancellor hopes that we would not feel obliged to accept such a deal. If we did, however, the outcome for 1983-84 onwards could be some £250-£350 million worse each year than the survey report implies, and the net contribution could be running at around £1 billion a year by the mid-1980s. The run of figures might then look something like this:-

	£ million			
	1982-83	1983-84	1984-85	1985-86
Net payments to EC institutions	635	725	800	1000

The Chancellor believes that Ministers will need to have the above risks in mind in the forthcoming discussions on the Survey. The existence of such risks must clearly affect the decision on the size of the contingency reserve for the later years.

An alternative way of allowing for the above risks would have been to construct the survey figures on a more pessimistic assumption. But this would have raised two problems. First, there is no clear basis for such an assumption. Second, it would have meant inviting Ministers to take decisions on one set of figures in the Survey and then to publish another in the White Paper. The White Paper will have, for negotiating reasons, to show figures based on the assumption of 66 per cent refunds with no extra adjustments for the so-called 'overpayment': the UK could not afford to signal to others in the Community a willingness to contemplate anything less favourable than this.

I am copying this letter to the Private Secretaries of Members of the Cabinet, and to David Wright in the Cabinet Office.

Yours ever,

J.B. KERR

12 July

E,

Pl. put this in the folder for the 'overhead' forward meeting – and a copy of the Article

CHANCELLOR OF THE EXCHEQUER

cc Chief Secretary
Economic Secretary
Financial Secretary
Minister of State (R)
Minister of State (C)
PCC
Mr Cassell
Mr Evans
Mr Britton
Mr Shields
Mr Riley
Mrs Lomax
Mr Sedgwick
Mr Barber
Mr Ridley
Mr French
Mr Harris

SAM BRITTAN - 'A FRAMEWORK FOR A STIMULUS'

You asked for my reaction to Sam Brittan's article "A framework for a stimulus" in the F.T. of 8 July. The article takes the following line,

(i) money GDP is growing at a lower rate than is consistent with the MTFS; whereas the MTFS was based upon a growth of money GDP of 9½-10 per cent the most recent movement of inflation and output points to a growth of only 8 per cent per annum

(ii) the authorities should fix as an objective a growth of money GDP of 10 per cent on average for the next two years

(iii) this leaves room for a stimulus - providing it is within the framework of the MTFS

(iv) a fiscal stimulus is preferable to a reduction of interest rates

(v) This fiscal stimulus should involve a reduction of NIS or VAT

2. I would summarise my reaction as follows,

(i) the framework of looking at money GDP is useful in assessing whether policy is operating with the appropriate degree of tightness. However the article puts too much stress on fine tuning this magnitude and

exaggerates the extent to which the government can offer the community a trade-off of x per cent growth for y per cent inflation

(ii) our assessment is that nominal GDP is growing a bit below the rate expected at the time of the budget but the difference is possibly only 1 per cent compared with Mr Brittan's estimate of 2 per cent. This forecast revision owes more to a lower than expected growth of exports and more rapid growth of imports than to a lower than expected growth of 'domestic' demand

(iii) Given the magnitude of the revision to the forecast and the reason for it I am not convinced that a fiscal stimulus at this point is appropriate. Instead I would prefer to continue the policy of reducing interest rates where possible and appropriate. Over the longer term, the conclusion that a reduction of labour costs is required to encourage the necessary amount of labour using (better described as 'capacity expanding') investment is consistent with the approach taken in the last Budget and could remain the priority next March. There may also be a case for announcing in the Autumn that from next April NIS will continue to operate at an effective rate of 2 per cent rather than revert to 2½% as is indicated by the present arrangements.

Money GDP and the MTFS

3. The Brittan article argues that instead of growing within the range of 8-12% money GDP is probably growing in the range of 6-10%. He obtains this estimate by combining official hints that this year's inflation rate will be lower than the official forecast of 9 per cent (he puts it at 8 per cent) with the outlook from CBI surveys of output growth of between 0 and 1 per cent.

4. The revision to the official forecast is rather less than this. The June forecast did revise downwards the growth of money GDP for 1982, but only by 1 per cent - from the MTFS figure of 10½% to 9½%. One source of confusion may be the revision to the inflation outlook. This has mainly been in the 'administered' components of the RPI, such as mortgage interest rates, and council house rents which do not affect the GDP deflator in the same way.

5. When examining the case for a stimulus a further relevant factor is the reasons for the revision to the forecast. This has primarily been because of a deterioration

in net trade. The weakening of exports can be partly explained by the worse world outlook but the import picture also suggests that a smaller than expected proportion of the increase in domestic demand is being met from domestic sources.

6. To highlight this problem it is interesting to compare the forecast expenditure figures for the first half of this year with those for the same period in 1981. Domestic demand is almost 4 per cent higher - mainly because of a recovery of private sector fixed investment and a virtual end to de-stocking. But exports are only a little over 1 per cent higher whilst imports are up by 11 per cent. The result is that output is only 0.7 per cent higher than a year ago. To an extent the rise in imports is a reflection of the nature of the increased demand; in particular stockbuilding has a high import content. But it also appears that a large proportion of the increased investment in plant and machinery is being imported. This all suggests that the problem of slow recovery is not easily characterised as a problem of inadequate domestic demand.

7. The growth of money demand over the past six months may have slowed to between 8 and 9 per cent per annum. But this can be largely attributed to the weak world level of output and the high interest rates operating last Winter. Now that nominal interest rates are significantly lower some pick-up is expected. Even so it is important not to make too much of relatively small movements of money GDP. The Brittan article implies a degree of fine tuning that is difficult to reconcile with a magnitude that is not easy to forecast; that is subject to considerable data revisions and can only be imprecisely influenced by policy instruments.

8. We discussed the role of a money GDP objective last year. As you know I see some merits for its use as a way of describing the objectives of policy and assessing the strength of policy at a time when financial indicators are giving conflicting signals. This is particularly the case when there are major institutional changes and innovations in banking technology. But there are problems as we found last year. Money GDP is the addition of inflation and output; this is not always useful for policy purposes when the objective is a reduction in inflation and an increase in output.

9. As Sam Brittan suggests it is presentationally useful to be able to argue that government policy is directed towards controlling the growth of nominal magnitudes but that the outcome for inflation and output is in the hands of private sector agents. But if you take this seriously, Government cannot logically go on to say, as he suggests: "we will do our best to ensure that if inflation does drop to 7 or 8 per cent then output will rise by 2 or 3 per cent. If inflation were to fall to 5 or 6 per cent output growth would rise towards 4 or 5 per cent".

Government can no more 'seek to ensure' 4% growth at 6 per cent inflation than at any other rate of inflation. Indeed it is part of the case for focussing on money GDP, as he himself has made it, that government cannot determine inflation and output separately in this convenient way. Government can attempt to maintain a growth of money GDP of (say) 10 per cent but, for example, if there was some tendency to undershoot this figure because of lower than expected inflation any policy response would affect inflation as well as output. On this view the most that can be said is that Government will attempt to maintain a growth of money demand of (say) 10 per cent. The division of that is up to the private sector and the higher the inflation rate the less room is available for real growth.

10. More generally it is important to recognise that the conditions for growth of output involve more than a reduction of inflation; it also requires the incentive to produce in the form of profitability and an adequate growth of world demand. A money GDP framework presented in the form proposed could go too far to lead people to think that all that is required for better output is a lower rate of inflation. In addition to lower inflation increased returns from investment are necessary if the output levels necessary to support higher levels of employment are to be achieved. And if world output is depressed this must limit the extent to which UK output can grow.

Size and Nature of Stimulus

11. Even though I have questioned the scale of the revision to the outlook this does not remove entirely the case for some easing of policy and it is important to avoid any further tightening. This is the approach that has justified the attempt to continue to reduce interest rates and the discussions you have held on the implications of trying to avoid being caught up in a higher level of US interest rates. The various financial indicators do suggest that financial policy last Winter was tighter than expected and the latest monetary figures are consistent with some easing of interest rates.

12. However there are two important qualifications. Inflation has fallen faster than expected in recent months and this has the effect of easing financial conditions for any given annual PSBR or money supply growth. The second qualification is that the outcome for public expenditure may be worse than assumed in either the MTFS or the latest forecast. This must be taken into account in any assessment of fiscal policy.

13. Sam Brittan argues for fiscal measures rather than for lower interest rates.

That choice may be affected by the scale of any action; and our (smaller) estimate of the room for manoeuvre may point more in the direction of interest rate changes in any case. But it is worth looking at the options again and the logic for the present approach.

14. There is widespread agreement that any policy action should be directed towards 'supply encouragement'. This means reducing UK costs and increasing profitability. Both interest rate reductions and the fiscal changes proposed in the Brittan article fall into this category. There would also be agreement on the need for 'capacity increasing' investment as well as 'productivity increasing' investment. This is where the choice of approach becomes more difficult.

15. VAT gets onto his list because it reduces labour costs indirectly as a result of lower prices. But the objections in terms of the tax structure are well known. It can also be argued that this is not the time for measures which reduce the inflation rate in the period immediately ahead but which are likely to raise inflation in the following period. This is because weak commodity prices are already having important temporary disinflationary effects. To combine this with other measures that would only have temporary effects would only help to reinforce the chances of a reversal on inflation.

16. The case for an NIS reduction is that it reduces employment costs directly. As we know the problems lie in judging the size of any offsets because of leakages into lower prices and higher pay settlements. A further complication is that NIS is relatively inflexible as it needs a long lead time. I remain attracted by the longer term arguments for NIS reductions. Poor cost competitiveness and the need to reduce employment costs make this a particularly inappropriate tax. But the time for assessing changes is in the context of the budget judgement when the competing uses for any scope for tax reductions can be examined. It is not a measure to be taken because of small deviations from the expected growth of output. The exception to this is that there may be a case for examining the possibility of an announcement in the Autumn that from next April NIS will continue to operate at an effective rate of 2 per cent rather than revert to 2½ per cent as is indicated by the present arrangements. By then we should know a little more about the prospect for 1983-84, especially the public expenditure plans. If action is not taken there will be an increase in the effective rate in April - or at least there appear to be one.

17. Interest rate reductions also reduce business costs although they do not directly reduce the effective cost of employment. But in my view Sam Brittan,

makes too much of this distinction in his article. It is true that labour substituting investment is more likely the higher are employment costs. But lower interest rates will also encourage capacity expanding investment. He mentions the fact that lower interest rates might bring a lower exchange rate. The effect of this may be considered to be ambiguous in the present context as it will simultaneously increase profitability and inflation. However real interest rates remain very high by the standards of historical comparison and there is a good case for a return to more normal levels. And we are not operating an exchange rate target as he assumes. Finally interest rates are particularly suitable for change within a financial year because of their flexibility.

18. The budget strategy in March was to do what was thought possible to reduce business costs by fiscal means. At the same time an overall PSBR was chosen to give the possibility of reducing the high level of real interest rates. Some progress has been made to reduce interest rates and there is further scope available if it is judged appropriate and still leave real interest rates at or above normal levels. There seems to be little case for changing that budget judgement at this stage particularly as the actual reduction in NIS has not yet taken place.

TB

TERRY BURNS

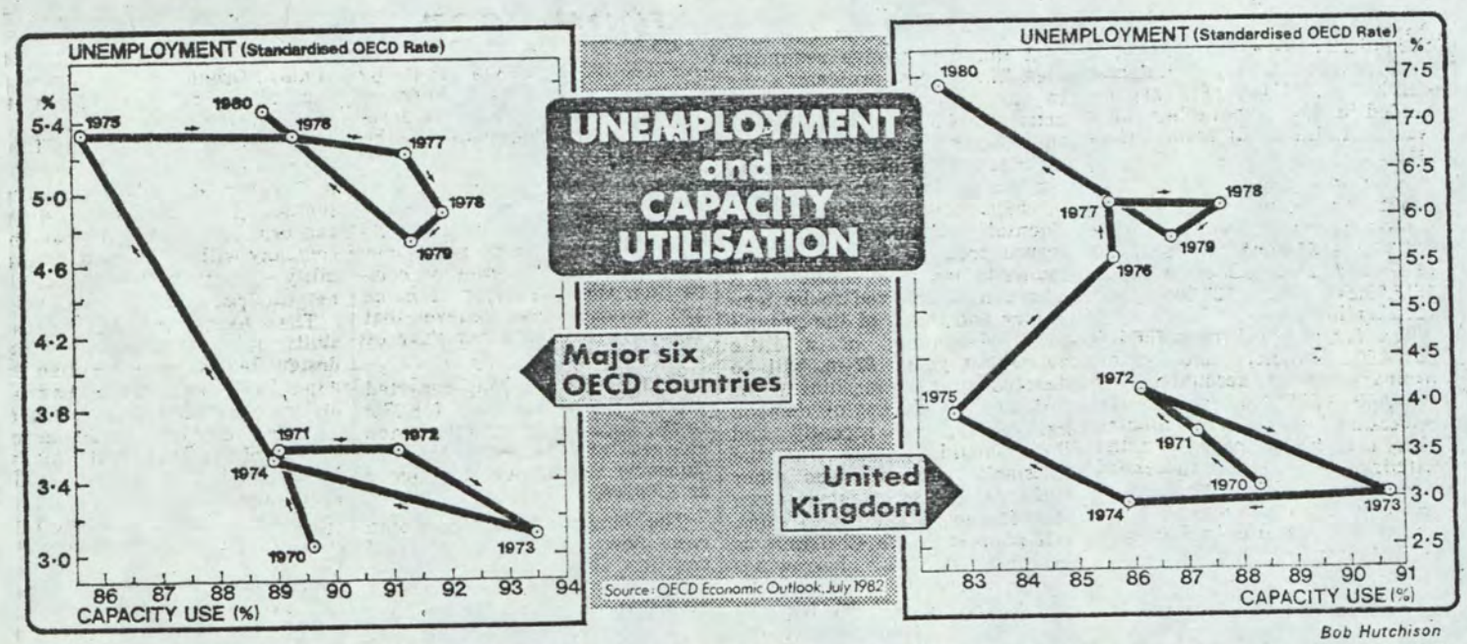
12 July 1982

Financial Times Thursday July 8 1982

ECONOMIC VIEWPOINT

A framework for a stimulus

By Samuel Brittan



Bob Hutchison

The high level of real interest rates is one among several pieces of evidence suggesting a shortage of potential capacity. The two "oil shocks," other changes in input prices, technical progress, and shifts in the composition of demand have all made a good deal of existing plant and equipment obsolete. The rise in the labour force in many countries has increased the capital shortfall compared with what is required for full employment.

The chart shows how, both in Britain and in the six main countries of the OECD combined (the U.S., Japan, Germany, France, Italy and the UK), a given degree of capacity utilisation has been associated with successively higher unemployment rates. For instance, an 82½ per cent degree of capacity utilisation was associated in the UK with an unemployment rate of 4 per cent in 1975, but one of 7½ per cent in 1980.

Thus the main bottleneck in the way of expansion may no longer be skilled labour, as in the past, but lack of adequate physical capital. The OECD concludes that an economic recovery which brought a return to past levels of capacity utilisation would not be sufficient to absorb the labour market slack.

The capacity index is based on a direct calculation by the OECD, based on factors such as past investment and relative price changes. It is not derived from business surveys.

THERE IS said to be an argument in the Treasury and the Bank of England between those advisers who want to take a risk with the exchange rate in order to reduce British interest rates and those who believe that a strong pound is an essential prop in the battle against inflation.

Those who want to reduce interest rates are thinking not only of the direct stimulus that lower interest rates would provide for activities such as stock-building and construction. Some among them also think that a lower pound would in itself be directly useful for the boost it would give to competitiveness.

Readers will have no difficulty in imagining for themselves the slogans used on either side of this argument. My own view is that it will never be resolved at the level of policy instruments and a shift is needed to the level of policy objectives.

Interest rates, exchange rates and fiscal policy are all instruments for influencing *demand*. It is not a bit of good becoming bogged down in an argument about means until we have made up our minds in which direction to exercise this influence. Some City and Conservative enthusiasts try to say (a) that we do not need a demand stimulus and (b) that interest rates must be lowered—as if the second were not above all a means to the first. This is a mirror image of the error of the U.S. Reaganites who argue on the fiscal side.

What is the main insight that should have been gained from the so-called "monetarist" counter-revolution? Not some dubious and ephemeral technical monetary proposition, but the much more important warning that it is impossible for governments to spend their way into target levels of output and employment irrespective of what is happening to wages and prices.

What is the main insight which we can retain from the Keynesian revolution at a policy-making level? It is that governments and central banks have a responsibility for stabilising the growth of *monetary* demand—that is total cash spending or Money GDP.

Jeremy Bentham once said that the opponents of the "Principle of Utility" ("the greatest good for the greatest number") were themselves unwittingly using that very principle in their arguments designed to refute it. Similarly nearly every rejoinder I have read to the proposal for a Money GDP objective contains statements which take this measure for granted as a criterion for stabilisation policy.

The matter is of immediate and practical relevance. Between 1979 and 1980 Money GDP was rising at average rates of 16 to 18 per cent per annum. Talk of inadequate demand or stringent financial policy rang very hollow during this period. Now, however, the Central Statistical Office has announced and highlighted the fact that Money GDP rose by only 10 per cent in the year to the first quarter of 1982. We now therefore have a genuine policy choice.

In the Budget "Red Book" a growth of Money GDP of 9½ to 10 per cent was projected for 1982-83 and a rate of only a couple of decimal points less was projected for 1983-84.

There is clearly a danger that money national income will grow by less than projected. There are many official hints that this year's inflation rate will be lower than the official forecast of 9 per cent. Let us put it at 8 per cent (which might be 7½ per cent on the "GDP deflator"). It also looks from CBI surveys and other evidence as if output will grow by between 0 and 1 per cent instead of the 1 to 2 per cent originally forecast by the Treasury. Putting the two sets of estimates together the most likely growth of Money GDP in fiscal 1982-83 could be somewhere around 8 per cent.

These seemingly precise figures are of course shorthand. What they really mean is that instead of the originally projected range of 8-12 per cent (which, not by coincidence, was also the objective for the different measures of the money supply) a growth rate for money GDP of 6 to 10 per cent is more likely. Even then the difference would not be worth bothering about, were it not that unemployment—even in terms of seasonally adjusted figures—is already nearly 3m and still rising at a rate of at least 30,000 a month: and there is no comfort to be drawn from vacancies, which are no higher than last autumn.

In unadjusted headline terms, the "shock" figure this July, when the school leavers arrive on the register, could easily be "Unemployment nears 3¼m" bringing the Government's second post-Falklands honeymoon well and truly to an end.

This is not a time to run any risks on the side of deficient demand growth; and it would be quite consistent both with "sound money" and new style Keynesianism for the Government to make its 10 per cent Money GDP growth projections if not into a target (a word which conjures up ridiculously precise expectations) at least into an objective for, say, the average of the next two years.

In other words it would be saying: "We will do our best to ensure that if inflation does drop to 7 or 8 per cent then output will rise by 2 or 3 per cent. If inflation were to fall to 5 or 6 per cent output growth would rise towards 4 or 5 per cent. This is not something we can achieve quarter by quarter, or guarantee at all, it is a trend towards which we can work." The other side of the coin is that real growth depends on wage and price moderation; the government's undertaking would be limited to money flows over which it does have an influence.

Obviously I am suggesting a stimulus (for the first time in well over a decade) but *in the context of a reaffirmation in convincing and comprehensible terms of the Medium Term Financial Strategy (MTFS).*

It would be all too easy to give a stimulus which was more than offset by pay and price increases — thus worsening instead of improving real demand and employment. A £2bn stimulus to monetary demand outside the context of the MTFS may be dangerously large, while a £5bn boost set convincingly in its context, might be well within the safety margin.

This last figure includes the demand-boosting effect of any interest rate reduction; and any citation of it without reference to the overriding importance of staying within the MTFS framework would be a cynical and politically motivated misrepresentation.

The possible stimuli fall into three classes: public expenditure or public works measures, which on some very mechanistic calculations provide the largest numbers of jobs; the interest rate-exchange rate measures canvassed in financial circles, and indirect tax cuts either of a VAT kind or of the employers National Insurance Surcharge (NIS).

Priority should of course be given to measures with a long-term employment-increasing potential. Interest rate reductions on their own may well stimulate labour-saving rather than labour-using investment. Moreover to the extent that interest rate reductions bring down the exchange rate, they will have an unfavourable impact on domestic prices and on inflationary expectations, and thus fritter away the boost to monetary demand.

Labour-using investment will be encouraged, as the OECD points out, by anything which reduces labour costs either relative to capital costs or relative to value added. This seems to argue strongly for the VAT-NIS range of measures. In contrast to exchange depreciation, they have the advantage of reducing prices and inflationary expectation and thus encouraging wage moderation.

It would be possible for a full year revenue cost of £3bn either to abolish the remaining 2½ per cent NIS completely or to reduce VAT from 15 to 12 per cent. The latter would reduce the RPI by 1 to 1½ per cent overnight and bring 6 per cent inflation within sight. The Chancellor's very sensible desire to abolish the annual wage round and make pay increases depend on individual circumstances might then no longer be a pipe-dream. Either measure should be affordable within the context of a reaffirmed MTFS providing for a 10 per cent growth of Money GDP, so long as interest rate cuts do not go much further than those already in the pipeline.

10 DOWNING STREET

(2)

From the Private Secretary

Prime Minister

Public Expenditure Cabinet

The objective is, clearly, to have as brief a discussion as possible about public expenditure on Thursday. We certainly want no repetition of last July's discussion.

The Chancellor is doing a lot of lobbying next week with that aim in mind. The one Minister he and the Chief Secretary can't lobby is Mr Nott. There is still a potential argument between the Treasury and MOD about the interpretation of the NATO 3%. This is

PTO

worth £1 billion over the Survey.

Should we try to do something about this before Thursday? Is there any intermediary whose ~~ca~~ assistance we could seek?

MCS 9/7

PRIME MINISTER

Prime Minister (2)

8 July 1982

MIS 9/7

THE PUBLIC EXPENDITURE DEBATE

MS

At the Cabinet discussion on Public Expenditure on 15 July, there will clearly be anxieties expressed about the modest rate at which output is recovering and the obstinately high level of unemployment.

It may also be argued that yet another "round of cuts" will do little to assist hope of economic revival.

It is tempting to defer a substantive discussion of these points, in view of the unhappy experience of the similar exercise last summer. Now that the Public Expenditure White Paper is published not in December but at the time of the Budget, there is certainly a case for not going into the recess on an acrimonious note. If the Treasury has no operational objections, it would be possible to start the whole exercise in September and still cover the ground thoroughly in good time. Postponement does, however, carry several risks:

(a) The press would get wind of the fact that the Cabinet had postponed meaningful discussion of the central issue. Indeed, the absence of any sparks flying would alert the newspapers to the postponement. This might be taken as meaning that the Treasury had ducked out of meeting the issue and that the Government was weakening in its commitment to the control of public expenditure.

(b) The same interpretation might also spread to the markets. Confidence is always hard to maintain over the financial "silly season". Without the Cabinet having left behind a clear indication of its unwavering determination, the summer holidays might well be an increasingly uncomfortable time. No doubt the position could be recouped somewhat in September, but vital ground might have been lost.

(c) In bilateral discussions with other departments, the Chief Secretary would be at a disadvantage, lacking any overall expenditure limit to back up the arguments for retrenchment. Experience may suggest that this overall limit is not final; even so, it is surely a useful reinforcement for the Chief Secretary.

(d) There is little reason to assume that the discussion would be any easier in the autumn. Indeed, the reverse, since some departments might have taken the delay as a signal to nudge their bids upward.

If well-defined public expenditure targets are to be established before the recess, it is essential to put the argument in a positive and political context. This public expenditure review is a central element in our plans to arrive where we want to be in May-June 1984 or October 1983.

Therefore, we should first remind colleagues of the important benefits to be gained by further restraint.

1. We all agree that falling interest rates are the best stimulant for recovery. Interest rates have now been falling steadily for more than 6 months. As inflation falls, we must retain this momentum, showing that British interest rates are and ought to be primarily determined by domestic monetary conditions and not by US rates and the defence of a particular exchange rate. Even the Daily Telegraph is now urging us to "decouple". But we can translate this attractive notion into action only if we are seen to stick rigidly to our targets for the PSBR.

2. Our aims for the 1983 Budget have to be kept firmly in mind at the start, and not left as a residual. We must index tax allowances fully. If possible, we would like to reduce taxes on low incomes to increase the incentive to work and to retain the loyalty of lower-income taxpayers who have done relatively poorly out of this Government. Beyond that, we wish also to have a modest amount in reserve to help specific industrial and other good causes. All this will require stringent control of public expenditure now if the books are to be seen to balance well enough to allow further falls in interest rates.

3. We are already committed to a huge expenditure on make-work employment subsidies and other methods of reducing the numbers on the employment register. Further such schemes are now in the planning stage. These schemes are of the highest political importance, and room has to be found for them in the Budget.

4. There is also a strong case for further help, apart from the reduction in interest rates, for the construction industry which has borne the brunt of the recession and has contributed so largely to the unemployment totals.

There is an increasing public dissatisfaction with the shabbiness of Britain. We expect our streets to be cleaner and our roads to be better maintained than in other countries. More and more people returning from holiday on the Continent make unfavourable comparisons. Potholed roads and collapsing sewers are a demoralising sight which may well exercise a subtle anti-Government influence. Such public works fall into a different category from many of the giant public investment schemes of which we are rightly so sceptical, such as rail electrification. First, they are essential works, whether financed by Government or, preferably, by private sources. Second, they cost more the longer the delay before tackling them. Third, they employ a great deal of unskilled labour which otherwise finds work hard to come by. Fourth, they can be contracted out to the private sector. A modest programme of rebuilding and cleaning up would have benefits out of proportion to the expenditure involved.

5. Above all, it is politically vital that we should keep inflation on a falling curve. Failing that, all the sacrifices will seem to have been wasted.

6. All these plus factors can be simultaneously achieved only by the most strenuous and unremitting control of public expenditure in all other fields. And this means, above all, maintaining the most stringent control of current expenditure, and in particular of public sector pay. It may help to remind colleagues that every 1% off the public service pay bill saves about £350m.

Each field bristles with difficulties. The Chief Secretary has already had to ask the nationalised industries to reduce their investment demands by £500m.

In social security, we have had the greatest difficulty in rolling back, even fractionally, the advance of indexation.

Defence - even regardless of the Falklands responsibilities - is now "super-indexed" because of the NATO 3% pledge.

We must not allow ourselves - let alone the outside world - to imagine that our series of public expenditure exercises, painful though they were, have succeeded in building in any permanent restraints on the growth of public expenditure.

We have had to back-pedal desperately and even so we have not managed to stay in the same place, and it is of the highest importance that everyone should understand this. Any suggestion that public expenditure is now a matter of secondary importance, which can be "put off until the autumn", would be highly damaging.

7. If we fail, the shape of the future is horrifyingly clear in the Treasury's study of Public Expenditure in the longer-term. The Chancellor estimates that, on a low-growth scenario, public expenditure might rise to no less than 46.8% of GDP by 1990/91 - a higher proportion than at any time since the disbanding of the War economy. Even on a somewhat optimistic assumption of 2½% growth per year, public expenditure would still be taking nearly 40% of GDP by 1990. And this omits the "creep" factor. Judging by all previous experience, the planning total tends to be added to as the year progresses. Cumulatively, outturn expenditure drifts upwards, setting higher base years for succeeding forecasts. The outturn for 1990 thus might be anywhere between 5-10% higher than the forecast If we continue to finance this level of expenditure honestly by taxing and not by borrowing, the implications for tax rates are extremely grim. If nothing else is changed and the money is to be raised out of direct taxation, a standard rate of 35p in the pound is a modest assumption. To avoid that intolerable prospect, we shall need to devise drastically new approaches to public spending.

8. But the long term starts now. And unless we continue to maintain - and intensify - our efforts to control public expenditure, there is every chance that we may be entering one of those periods, such as the early 1960s and early 1970s, when public expenditure simply gallops out of control.

Both Tory periods!

FERDIN

AW

ALAN WALTERS

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10 DOWNING STREET

From the Private Secretary

8 July 1982

CABINET, 15 JULY

Thank you for your letter of 6 July, to which were attached three draft Cabinet papers: the Chancellor's on the economic background, the Chief Secretary's on the objectives for the 1982 Survey, and another by the Chief Secretary on "End-year flexibility".

As you know, the Prime Minister and the Chancellor discussed these en route for Rome. The Prime Minister has agreed that the three papers should be circulated, and that the first two should be discussed at Cabinet on 15 July; on the flexibility paper, she would prefer no discussion either on 15 July or before the recess.

I am sending a copy of this letter to David Wright (Cabinet Office).

M. C. SCHOLAR

John Kerr, Esq.,
HM Treasury

CONFIDENTIAL

Prime Minister (1)

Agree to the circulation of these three papers?

Would you prefer the end-year flexibility paper to be discussed some time after July 15? Yes MT

MCS 6/7

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

6 July 1982

Michael Scholar, Esq.,
10, Downing Street

Dear Michael,

CABINET : 15 JULY

..... I enclose copies of three draft Cabinet papers, i.e.

(a) The Chancellor's paper on the economic background

(b) The Chief Secretary's paper on the objectives for the 1982 Survey

(c) A short paper by the Chief Secretary covering an interdepartmental report on "End-year flexibility".

The Chancellor envisages that the first two would be circulated this week for discussion on 15 July.

His own paper sets the scene, along lines which will be familiar to the Prime Minister from their recent discussions. Its scope is wider than the public expenditure issues, and the Chancellor in fact believes that it would be useful for the discussion on 15 July to be fairly wide-ranging. But it also points to the importance of holding the public expenditure planning totals.

This is the Chief Secretary's aim in the survey, as set out in his paper. The Prime Minister will remember that the totals were increased, by £5 billion for 1983-84, and £7 billion for 1984-85, in the last Survey. The reasons for opposing any further increase are set out in both papers. But the Chief Secretary is not seeking a cut in the overall level of public expenditure: the objective is to maintain the present planning totals, offsetting increases in one programme against reductions in another.

The Chief Secretary has yet to decide whether to circulate the third paper this week. It presents a report commissioned originally by OD in February, and (by mutual consent) postponed until the public expenditure round. It sets out the arguments for and

/against

against various schemes of end-year flexibility. The Chief Secretary's covering paper comes down against such schemes, particularly for this year. There is no doctrinaire objection to end-year flexibility (and indeed something to commend it). But schemes of this kind are not strictly necessary: if Ministers collectively decided to take note of an underspend in one year, and add a corresponding amount to a particular public expenditure programme in the following year, the usual mechanisms (Supplementary Estimates and a call on the Contingency Reserve) are already there. The proponents of end-year flexibility want a completely automatic system. Treasury Ministers are reluctant to concede full automaticity, and point out that the costs are likely to be high.

The Chancellor feels that it would be a pity to waste much time on the third paper in Cabinet on 15 July. It could perhaps be taken fairly summarily at a later Cabinet this month. But if the officials' report had not been circulated by 15 July Cabinet colleagues might then enquire about its fate. The Chancellor would welcome advice on how the Prime Minister would like this to be handled.

A copy of this letter goes to David Wright in the Cabinet Office.

Yours ever,

J.O. KERR

DRAFT

ECONOMIC PROSPECTS

The economic situation has not changed dramatically since the Budget, though the outlook for US, and so world-wide, growth has worsened, while the prospect for inflation here has improved.

Prospects

2. Over the next two years the prospects seem to be:-

(a) World Outlook. The fall in US output stopped in the second quarter, and there should be some resumed world-wide growth in the rest of this year and throughout 1983; but the level of world activity is likely to remain lower than we had earlier hoped. Oil prices are higher than we had assumed at Budget time: this improves our revenue take, though the effect on inflation is of course adverse.

(b) Output. Our recovery has shown some hesitation in recent months, due to weaker trading conditions in many industrial countries and the temporary rise in interest rates at the end of last year. But the forward indicators point to a perceptible, though perhaps uneven, rise in output over the next year. The latest forecast is for 2 per cent growth in 1983.

(c) Unemployment. The growth in output is unlikely to be fast enough to reverse the rising tide of unemployment, but may be sufficient to arrest it. We have to reckon on unemployment, on the wide definition, remaining around 3 million. Levels are rising steeply in our competitor countries.

(d) Interest rates have fallen by about 3½ points since last autumn, but further falls may depend on what happens in the United States, where rates, both nominal and real, are well above ours; and on our maintaining confidence at home.

(e) Prices. Inflation has declined more rapidly than expected. The Budget forecast was for 9 per cent by the end of this year and 7½ per cent by the middle of next year. In fact we now expect to hit 8 per cent by the end of this year, and about 7 per cent by the middle of next year. On past experience there must of course be a risk that, as the economy picks up, so too will the inflation rate. We need to do all we can to prevent this: continuing success on the pay front will be one key element.

3. These indicators from the latest Treasury forecast are summarised in the attached table. As we approach the next election we should be able to point to an economy which is again growing (though with unemployment still very high); to major progress on inflation; to substantial achievements in productivity and competitiveness; and to considerable success in insulating ourselves from the pressures caused by high US interest rates. In short, our attack on the fundamental malaise of the British economy is making progress and deserves to be sustained.

Hazards

4. This scenario is however at risk in a number of areas.

5. First, developments abroad. There remains a strong risk that US interest rates will remain high - and could indeed go higher. And we cannot rule out the possibilities of international financial disorder deriving from major loan defaults, private banking failures, or exchange rate volatility.

6. Second, the domestic pay scene. E Committee is discussing this: the key point is that another pay explosion could blow away much that we have achieved, on inflation, productivity and competitiveness. We need settlements in the coming pay round substantially lower than those in the one now ending.

7. Thirdly, and perhaps most important, we could, by omission or commission, lose the confidence of the markets, domestically and abroad. This could result from a bad pay round, but equally it

could spring from any suggestion that we were relaxing our grip on public expenditure, or that we were prepared to reverse engines on the drive to reduce borrowing, or through failure to carry conviction about our determination to maintain non-inflationary monetary conditions. Loss of confidence for any of these reasons would affect the recovery through the exchange rate, and interest rates, and more generally.

The Budget Prospect

8. At the time of the last Budget we saw room for tax reductions (over revalorisation) of only some £0.5 billion in the financial year 1983-84, assuming that the spending totals were held. This would be significantly less than we were able to concede in the last Budget; and the latest forecast does not materially change the position. Yet the case for assisting recovery by further tax reductions, for industry and if possible by raising personal tax thresholds, remains very strong.

9. To adopt the ostensibly "easy" course of borrowing more in order to permit tax reductions would be fatal to confidence. We must hold to the plans for reductions in the PSBR as a proportion of GDP which we have announced and so far delivered. The US example demonstrates all too clearly the consequences of failure in this respect.

10. The 1981-82 PSBR was £1½ billion below forecast. Analysis however suggests that this shortfall will not be carried through into subsequent years. It has been taken into account in the latest forecast; which shows the PSBR this year and beyond remaining very close to the figures published at Budget time.

Paragraph

11. But this depends on holding, as the Chief Secretary proposes (C(82)), to the present spending plans, published only 4 months ago. If we were seen to be revising them upward, the effect on market confidence would be substantial and adverse.

12. Moreover, to increase the planning totals would mean a real possibility of tax increases next year. And to maintain market

confidence, we would have to make it plain that we would not shrink from such increases. Yet the fact is that they would be wholly inconsistent with what the economy needs, and what we have in the past promised.

13. Far better to avoid all this. As paras 2 and 3 above show, our monetary and fiscal policies are now starting to bring success; to change course would risk throwing away all that we have achieved, particularly on inflation.

Positive Action

14. But, though I am confident that we are on the right course, and must stick to it, we shall want to consider if there is anything we can do to improve the pace.

15. I am clear that we must be seen to do more to counter unemployment. This does not mean a change of macro-economic policy, for today's dole queue is not the result of our efforts to reduce inflation, but rather that of others' past failures to do so. To drop our efforts wouod merely store up new problems for the future, and would have a confidence back-lash. But we need a drive to make sure that what is now being spent, e.g. by the MSC, or what has already been made available, is being deployed to maximum effect, and attracts maximum attention. And we need to keep the political initiative in overcoming, or at least exposing, trade union resistance to sensible low-cost schemes for getting people off the register and into useful work.

16. Nor have we yet done enough to publicise and effectively promote all the changes we have made in order to encourage enterprise. A new publicity campaign has been agreed, but the search for ways of eliminating obstacles to enterprise must also be stepped up. There are major economic and political prizes to be won here.

17. Thirdly, on industry's costs, our role is two-fold. As well as working to secure further interest rates reductions (by ensuring that monetary conditions remain appropriate, seeking further to

insulate our markets from the threat of another US interest rate crisis, and helping to improve industry's access to medium-term finance), we need to encourage the further reduction of unit costs. This is not merely a matter of encouraging restraint in pay: industry must also be encouraged to go on improving efficiency, through investment and the necessary changes in working practices. This entails our supporting those whose efforts to secure higher productivity lead to industrial action, and stepping-up our efforts to secure the removal of institutional and other obstacles to changes in working practices.

Conclusion

18. The economic prospects as we approach the last part of this Parliament are not unpromising (paras 2 and 3), but there are risks (paras 5 to 7). The greatest, and the one most within our power to avoid, is that of allowing ourselves to be sucked into a spiral of higher expenditure, and therefore higher tax (paras 8 to 13). We must maintain our fiscal and monetary policies, so as to be able to go on bringing interest rates down, and this means maintaining our grip on public expenditure, Consistent with that, we can and must do more (paras 14 to 17) to combat unemployment, unleash enterprise, and help industry improve its competitiveness.

PUBLIC EXPENDITURE: OBJECTIVES FOR 1982 SURVEY

We now need to start considering the public expenditure programmes for 1983-84 and the two following years. The Report of the Public Expenditure Survey Committee (PESC) which gives the material is available in Departments.

The Aim

2. The aim which I propose is to hold to the present planning totals, that is, for 1983-84 and 1984-85 the cash totals for the aggregate of programmes plus contingency reserve which we agreed last November and published in the March White Paper, as modified by the decisions announced in the Budget and with some minor estimating changes. For 1985-86 there is no cash programme yet. In discussion of colleagues' programmes for that year, consistently with the aim I am suggesting for the previous years, I propose to aim for the total currently shown in the PESC baseline.

3. The present planning totals for 1983-84 and 1984-85 stand at £120.3 billion and £127.6 billion. These totals include the additions of £7 billion and £5 billion respectively which we agreed last year on top of the previous plans which had been converted to cash using general inflation factors of 6% and 5%. For 1985-86, the PESC baseline is £133.3 billion.

4. To hold to these plans should leave room for modest tax reductions next year, which could benefit industry and aid economic recovery. The economic prospects are discussed in the separate paper C(82).. by the Chancellor of the Exchequer. We must beware of new commitments which would add to our problems after the next Election.

The problem in 1983-84

5. To achieve the aim of holding the planning totals will be difficult. We can accommodate some limited additions to certain programmes by committing now some of the contingency reserves of £4 billion for 1983-84 and £6 billion for 1984-85. But we must keep an adequate reserve for unforeseen contingencies. The need to do this has of course been particularly vividly demonstrated by the Falklands experience. At the beginning of the current year 1982-83 we had a reserve of £2.4 billion, and already it is clear that we shall find it hard to live within this.

6. For 1983-84 we have to recognise the probability of a substantial increase in local authority current spending, simply because, even with a very tough RSG settlement, we have no means of preventing some increased spending occurring, however much we may deplore it. In addition it looks as if our statutory social security commitments will cost £0.6 billion more than is allowed for in current plans. Including these amounts, the proposals put forward so far during the preparatory work for the Survey already amount to about £6 billion extra for 1983-84 and about £7¾ billion for 1984-85; a summary of the main item is at Annex A. The Falklands will require certain additions to present programmes. So holding the planning totals will mean offsetting savings in some programmes.

Inflation

7. This year's Survey is the first to be carried out in cash at all stages. As I have indicated, the baseline figures originally incorporated an overall provision for inflation (pay and other prices together) of 6% in 1983-84 and 5% in 1984-85. The latest forecast for overall inflation, not just in the public sector, is about 7% for 1983-84, but I shall report any revision in September. No precise forecast can usefully be made for later years, but it will remain our firm objective that the rate of inflation should continue to decline. In these circumstances I propose no general revaluation of the cash programmes. In the case of public services pay, which we have discussed separately, we shall certainly want to aim at very much lower figures, and if later in the year our decision is to allow for less than the present implicit 6% for pay increases next year, it may then be necessary to make appropriate adjustments in the relevant programme figures.

Civil Service Manpower

8. The PESC Report this year sets out the approved and proposed manpower figures for each department. We are on course to achieve and hold the 1984 target of 630,000 civil servants. The position is tight. Any significant increases above what is now proposed would frustrate achievement of the 1984 target. There is no room for any new initiatives with sizeable manpower implications in the lifetime of this Parliament.

9. I propose that we now regard the figures in the Report for 1 April 1984 as firm limits in the next stages of the Survey. Within these limits, I will take up points with colleagues where some further reduction seems possible by April 1984 or where their figures for April 1983 seem too high to leave a feasible last step to their target for April 1984.

Conclusion

10. I invite the Cabinet:

(1) to agree that our aim should be to hold to the present planning totals for expenditure in 1983-84 and 1984-85;

(2) to note that this means only the minimum inescapable additions to programmes in the course of the current Survey, and requires reductions in certain programmes in order to leave room for these inescapable additions;

(3) to agree that the civil service manpower totals for 1 April 1984 proposed in the report should now be regarded as firm limits;

(4) to agree that within the general framework of (1) & (2), I should hold bilateral discussions with spending Ministers about additions and reductions to their programmes and report back to Cabinet in October.

ANNEX

BIDS FOR ADDITIONS TO PROGRAMMES IN 1983-84 AND 1984-85

The main bids received so far are as follows.

	1983-84		£m 1984-85
Defence	526	Including Armed Forces Pay, 3% real growth and relative prices	1200
	[250+]	Falklands consequences excluding garrisoning+	[250+]
Industry	272	Mainly regional development grants and launch aid for civil aircraft/engine.	400
ECGD	218	Effect of higher interest rate assumptions on export subsidies.	-
Housing	980	To maintain capital at 1982-83 level assuming rent increases in line with RPI.	825
Health	397	Inflation, relative prices, demography, health authority capital and some improvement in service.	532
Social Security	810	of which £560 million in 1983-84 and £661 million in 1984-85 for existing statutory obligation.	1233
Nationalised industry	1136	Increased external financing	1130
Local authority current	1100	Guess at likely expenditure over plan.	1250
Other	560		180
	6250		8000

+Provisional and partial estimate - not in PESC report

6/7

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CABINET

END-YEAR FLEXIBILITY FOR PUBLIC EXPENDITURE PROGRAMMES

Memorandum by the Chief Secretary

I was asked by the Defence and Overseas Policy Committee on 27 January to arrange for proposals for a scheme of flexibility between years for public expenditure. The invitation arose in the context of difficulties which were then anticipated with the defence programme, but the issue affects other departments too. The Secretary of State for the Environment subsequently suggested that we should consider end-year flexibility as a way of encouraging the construction industry.

2. I now attach a report by officials. As it reminds us, we have considered these questions before.

3. End-year flexibility would allow departments to carry-over any underspending into a subsequent year, or to overspend a cash limit in anticipation of a subsequent year's provision, or both.

4. Allowing overspending would be utterly inconsistent with our established policy that cash limits are a firm and effective control. I do not see how we could possibly support an arrangement which would appear to encourage or condone overspending of cash limits.

5. Allowing the carry-forward of underspending might be helpful to good management (though I think it is possible to exaggerate this). But it would also add to total public expenditure. The Treasury view is that the cost of the limited scheme described in paragraphs 19-20 of the paper would be of the order of £300 to £450 million a year starting in 1984-85. More ambitious schemes would cost more.

6. In the context of the situation described in my other paper C(82) , I do not think that we can at present afford any such scheme.

END-YEAR FLEXIBILITY FOR PUBLIC EXPENDITURE PROGRAMMES

Note by officials

The Defence and Overseas Policy Committee invited the Chief Secretary on 27 January to arrange for proposals to be submitted for a scheme of flexibility between years for public expenditure programmes, in time for possible introduction in 1982-83. Subsequently, the Secretary of State for the Environment suggested that consideration should be given to a similar scheme as a way of encouraging the construction industry. This paper, which has been agreed by an interdepartmental group under Treasury chairmanship, responds to both remits. It discusses the main issues and outlines the main points for decision should Ministers decide that they wish to implement a scheme of this kind.

History

2. End-year flexibility has been discussed several times in the recent past. In July 1980, the then Chief Secretary circulated a paper outlining a scheme which would have permitted carry-forward into a subsequent year of underspending on capital or equivalent programmes of up to 5 per cent. The scheme was discussed with the PAC, who indicated that they favoured a controlled experiment to provide evidence of its effectiveness (14th Report, Session 1980-81). In February last year, however, Ministers decided not to implement the scheme either in 1981-82 or 1982-83 because the potential cost in terms of additional public expenditure - £300 million in the first year and £450 million in later years in 1982-83 prices - could not be afforded. A description of the 1980 scheme, and its costing, is provided at Annex 1.

3. The Chief Secretary's scheme was a general one. Arrangements for certain types of end-year flexibility already exist within some programmes. In particular, individual local authorities already enjoy considerable flexibility for most of their capital expenditure, and individual health authorities for both current and capital expenditure, within the framework of overall national cash limits subject to the same discipline as any other cash limit. Flexibility arrangements of different kinds also exist for overseas aid and for nationalised industries' borrowing. A brief description of each of these schemes is provided at Annex 2.

Why end-year flexibility?

4. The objectives of end-year flexibility schemes are related to managerial efficiency problems associated with the strict application of annual cash limits. In brief they are intended:

(i) to reduce the underspending which tends to result from programme managers' actions to reduce the risk of overspending, especially in situations where the pattern of expenditure or receipts cannot be controlled precisely.

Persistent and significant underspending may be regarded by Parliament as symptomatic of bad management. It cannot, however, be avoided if annual cash limits for some of the programmes most difficult to control are to be strictly obeyed. The gap between declared plans and performance, particularly for capital programmes which the Government has stated it wishes to preserve, confuses Parliament and the private sector industries concerned. The respect for controls of programme managers set impossible targets is also undermined. On the other hand, although not always made explicit a general allowance for underspending is built into the Treasury's assessments of public expenditure and expected by informed commentators. If this were reduced, planned expenditure on programmes would, other things being equal, have to be lower to keep within the same planning total.

(ii) to reduce the risk of waste at the end of the year. As the possibility of underspending becomes apparent, low priority expenditure with a short lead-time may be brought forward to reduce it.

The extent to which waste of this kind does take place is a matter for debate. The evidence is mainly anecdotal. It certainly does happen. But it does not necessarily follow that items brought forward because of short lead-times are not desirable in their own right.

(iii) to reduce the risk of waste throughout the year, but especially at the end, if managers have to reduce expenditure quickly in whatever way they then can so as to avoid or reduce a threatened overspend.

Waste of this kind undoubtedly occurs from time to time, particularly in programmes where short-term cash flow can neither be controlled nor forecast within fine limits. This is true of the roads programme and complex programmes, like defence, where it may be impossible to adjust efficiently within an annual timescale. The problem is made worse where systems of forecasting, monitoring and control are inadequate.

5. Against these objectives have to be set the difficulty of cost, which could be very substantial depending on the precise nature of the scheme adopted, and the possibility of undermining the basic disciplines of cash planning, particularly if the scheme adopted covered overspending as well as underspending.

All these considerations have to be set in the context of the financial management initiative. Many departments believe that the drive to improve financial management and efficiency could increase the need for some kind of end-year flexibility if freedom and authority over their costs and expenditure is to be increasingly delegated to line managers. The right to accumulate savings in current expenditure to defray future cost-saving purchases, for example, could create difficulties if there was no corresponding freedom to carry voted funds forward into a future year. The Treasury do not, however, accept this. They believe that it is possible to exaggerate the extent to which strict observance of an overall cash limit is inconsistent with greater delegation of responsibility. It is already open to individual departments to provide flexibility between years for individual cost centres within their programmes (following the analogy of the health authorities and local authorities), provided the results can be contained within their total budgets. The introduction of better financial planning and control systems ought to make arrangements of this kind easier.

7. The following paragraphs briefly discuss the main issues which need to be decided if a scheme is to be implemented - whether it should cover over as well as underspending, whether it should include current as well as capital expenditure, which spending authorities should be included and the mechanics of the scheme.

Over and underspending

8. Most spending departments believe that end-year flexibility ought to apply to over as well as underspending. That is, they believe that spending managers ought to have the ability to anticipate up to a given proportion of a subsequent year's allocation, as well as to carry forward underspending into a subsequent year. They argue that only a symmetrical approach of this kind would fully meet the objectives set out in paragraph 4. The Treasury and Sir Derek Rayner's office take a different view. Considerations of cost apart, they accept that there may be case in principle for allowing the carry-forward of underspend. But they believe that to allow overspending in anticipation of next year's provision would seriously undermine the discipline of cash limits and cash planning. There would also be a problem of credibility, as to whether overspending would in practice be fully clawed back. A symmetrical scheme could be significantly more expensive in a given year than one confined to underspending.

9. It is already established policy that overspends on a cash limit in one year are automatically deduced from the cash limit for the following year.

10. The PAC did not recommend in favour of a scheme which allowed overspending. But they did suggest that the Government should consider whether in certain circumstances a 'less censorious' attitude towards occasional breaches in cash limits might be appropriate,

where this occurred beyond the control of departments. In their reply, the Treasury firmly rejected this idea.

Capital and current expenditure

11. The problems described in paragraph 4 apply mainly to certain capital and procurement programmes such as roads, defence procurement and prison building where much of the expenditure in a particular year may be on projects already under contract and where the timing of work and of payments for it may be uncertain. The problems of defence procurement were described in the memorandum by the Secretary of State for Defence circulated as OD(82)3. The difficulties of the roads programme are described in Annex 3.

12. Similar problems could, however, occur with certain types of current expenditure, particularly in areas where capital and current expenditure (as presently defined) are close substitutes for one another, or with R & D. The generality of current expenditure ought however, to be forecastable and controllable within much tighter limits than most capital expenditure.

13. Implementing a scheme to cover current as well as capital expenditure would add considerably to the cost. Total current expenditure by central government on goods and services in 1982-83 is planned to be £36 billion.

14. In practice, if a scheme was to be confined to 'capital and equivalent expenditure' this may need to be done in a way which meets the spirit of the proposals, even if it violates current accounting practice. The details of the expenditure to be covered on each programme would need to be discussed bilaterally once the decision as to principle had been taken.

Spending authorities to be covered

15. It was left open whether the 1980 scheme should apply to capital expenditure by local authorities and health authorities as well as by central government departments. It would be for consideration whether any scheme introduced now should do so. Individual health authorities and local authorities already have a great deal of flexibility within the national cash limits.

16. The arrangements for health authorities predate the introduction of cash limits. These appear to have worked well and to have given the health authorities the kind of managerial advantages now sought for central government departments.

17. The scheme for local authorities was only introduced in 1981-82. In that year the overall cash limit was underspent by around £600 million. The DOE believe that

derspending was partly caused by deliberate caution on the part of the local authorities, in turn partly caused by fear that the flexibility allowed them could lead to aggregate overspending, followed by a moratorium, as proved necessary for housing investment in 1980-81. Fears of this kind could be eased by a scheme which allowed for carry-forward at national level, particularly if it covered overspending.

Mechanics

18. There are a number of different ways in which a scheme for end-year flexibility could be operated.

19. The 1980 scheme was an administrative one. A similar scheme instituted now, and confined to underspending, might have the following features:-

(i) carry-forward to the following year of underspends, subject to a minimum (necessary to avoid an unmanageable multiplicity of small amounts; the nature of the minimum to be considered further but possibly a combination of a percentage and an absolute amount) and subject to a maximum percentage of the original capital programme: the 1980 had a maximum of 5 per cent. The Secretary of State for the Environment has suggested that it should be as high as 20 per cent.

(ii) the amount carried forward to be added to the programme previously settled for the following year and to be charged to the Contingency Reserve in that year, the Reserve being debited as soon as the amount carried forward is identified and agreed.

(iii) Supply estimates increased when required by way of supplementaries.

(iv) The system would probably only be workable if applied to whole cash limits. However, many cash limits contain a mixture of current and capital expenditure. It would be necessary to consider further the implications of this, including for the defence block budget.

20. A more detailed illustration of how such a scheme might operate is given in Annex 4. It could be introduced in 1982-83, with no credit being allowed for underspending in 1981-82 because by the time the scheme was launched it would be too late for it to produce any managerial advantages in that year.

21. An analogous arrangement could be devised to deal with overspending, though there could be problems of Parliamentary authorisation in relation to the overspending, in that it

ould increase the number of Excess Votes unless it emerged early enough for Spring Supplementaries to be taken. There could also be difficulties in managing the Contingency Reserve, since the possibilities of overspend may not emerge until very late in the year.

22. The MOD are concerned that an administrative scheme of this kind would not guarantee that flexibility would be allowed, since it would open to Ministers in any year to decide to refuse to agree to the necessary supplementaries (if, for example, they took the view that the Contingency Reserve could not accommodate them). The MOD have therefore suggested that, now cash limits are now mainly accommodated to votes, flexibility could also be voted if Parliament voted funds for a longer period than twelve months. Underspending could be catered for by allowing funds unspent at the end of March to be utilised during April. Overspending could be dealt with by allowing funds voted for the subsequent financial year through the vote on account to be utilised at the end of the previous financial year, e.g. from 1 March. In short, Parliament would vote funds for 14 months rather than 12. Underspent funds would automatically be carried forward for one month without creating a need for Supplementary Estimates in the following year. Overspending would automatically eat up the following year's funds and the cash limit discipline would be seen to be biting effectively. It would be for consideration whether a limit of some kind should be applied to the facility.

23. A fuller description of this alternative, as it might apply to MOD, is at Annex 5. It would probably require legislation, and could not therefore be introduced in 1982-83. It could involve a number of practical difficulties. Parliament could be expected to argue that Supply Procedure is already sufficiently flexible to allow the transfer of expenditure from one year to another without the need for devices which weaken their control over expenditure; and that the problem is one of public expenditure control, not Parliamentary authority for the issue of the necessary funds.

24. A third possibility would be to enable the payment of bills to be delayed or advanced to meet developing overspends or underspends. The superficial attraction of shifting payments in this way is that the cash limits of each respective financial year would remain unaltered; a potential underspend, for example, would be avoided by accelerating payments rather than adding to the following year's cash limit. Manipulation of bill payment would be in line with much private sector practice, and might be presented as a means of allowing more administrative discretion than the present situation allows.

25. Such a scheme would, however, require a change in the long-established principle that the Government pays its bills as soon as they are presented and the necessary formalities completed. They are good reasons for the convention. Deferring payments penalises firms and contractors - possibly unevenly - and would inevitably attract criticism. The Exchequer

would effectively be borrowing from the contractor. This would normally in some way entail an additional cost. Making payments in advance of due dates in order to avoid an underspend might be unobjectionable from the contractors' point of view, but would involve an additional borrowing cost to the Exchequer.

26. A change of this kind, would also raise practical difficulties. In particular, there would be uncertainty about the extent to which payments should be advanced or retarded. The problem of making outturn conform to cash limits would therefore not be resolved, though it would be reduced.

Cost of the schemes

27. The potential cost of introducing a scheme of end-year flexibility is very uncertain and would depend upon the detail of the scheme adopted. Two effects need to be considered - the effect on public expenditure totals and the improvement in efficiency which might result. The latter is very difficult to evaluate.

28. The potential future expenditure cost of the 'basic' scheme described in paragraph 19 is roughly estimated to be similar to that of the 1980 scheme, about £300 million to £450 million a year in 1982-83 prices, starting in 1983-84, if the maximum carry-forward is limited to 5 per cent. The cost in any one year depends on the balance of expenditure brought forward from the previous year and carried forward to the following year. There would be no cost, and possibly some saving, in 1982-83. A fuller explanation of the costing is provided in Annex 1.

29. Extending the scheme to cover current as well as capital expenditure or over as well as underspending could add substantially to the potential cost and to the variability of the effect on public expenditure in any one year. So would any increase in the margin of flexibility to be allowed.

Conclusion

30. Ministers are invited to consider whether they accept the arguments in principle for some form of end-year flexibility, whether they are prepared to accept the potential addition to public expenditure in 1983-84 and later years when measured against other competing priorities and, in the light of this, whether they wish officials to undertake further work in designing a scheme either for general application or a more limited experiment.

31. If further work is to be done, it would be helpful to have a guidance on:

(i) whether the scheme should be addressed only to underspending or should cover overspending as well.

(ii) whether it should extend to current as well as capital and equivalent expenditure.

(iii) whether it should cover the expenditure of health authorities and the capital expenditure of local authorities as well as the expenditure of central government.

(iv) which of the approaches outlined in paragraphs 18 to 26 they favour.

ANNEX 1: COSTING OF THE 1980 SCHEME FOR CARRYING-FORWARD OF UNDERSPEND

The scheme was limited to expenditure for which there is a managerial case for flexibility, principally capital expenditure. The carry-forward was subject to a maximum of 5 per cent of eligible expenditure and a minimum of 1 per cent, the minimum threshold being intended to prevent a large number of Supplementary Estimates for small amounts. Departments were asked to give their views on the scheme at official level and to give the total value of expenditure that would be eligible in 1981-82. It was explained that it was for consideration with the relevant departments whether it would extend to the capital programmes of the local authorities or the health authorities. The scheme would not apply to the external finance of the nationalised industries about which separate discussions were in progress. It was envisaged that the additional expenditure needed for the scheme would be charged to the Contingency Reserve and in evidence to the PAC the Treasury said that the carry-forward could be authorised in summer Supplementary Estimates.

2. Under this scheme the total of eligible expenditure was about £10 billion in 1980 survey prices, this figure including some allowance for local authority and health authority expenditure. Of this, almost £5 billion was on defence procurement and capital expenditure. In evidence to the PAC, the Treasury said that 'On a five per cent basis, the maximum potential carry-forward would be of the order of £500 million, but because departmental requirements would be uneven the actual carry-over should be less than that'. It was estimated that the actual carry-forward might be only about £300 million in 1980 survey prices. However, it was expected that the scheme would cause Departments to underspend slightly more because they would not be so anxious to spend their full allocations before the year-end and a figure for this effect of £100 million or so, in 1980 survey prices, was suggested.

3. The net overall cost of the scheme in the first year of operation would therefore be the £300 million likely carry-forward less the estimated £100 million additional underspend ie £200 million in 1980 survey prices. The scheme would have started with a carry-forward from 1980-81 to 1981-82, the net cost being about £250 million in 1980-81 prices, the rough equivalent of £200 million in 1980 survey prices. In later years the cost of the scheme would be higher since the higher underspend would be offset by the higher carry-forward, so the cost would be about £300 million in 1980 survey prices. In 1982-83 prices the cost would be £300 million in the first year and £450 million in later years.

4. The scheme considered in this paper is slightly different from the 1980 scheme in that departments would be given notice of its introduction; ie they would be told in 1982-83 that a carry-forward would be allowed from 1982-83 to 1983-84. So in 1982-83 there would be a

ving of about £150 million and in future years the cost would average about £450 million in 1982-83 prices with the cost being higher in some years, lower in others. The effect on the Contingency Reserve would depend on when the debits take place. If the carry-forward was authorised in summer Supplementary Estimates, the cost to the Contingency Reserve when the scheme is in operation would be £600 million in 1982-83 prices, which would be offset by an underspend of £150 million. However, if the debits only take place when departments need the money then the cost to the Contingency Reserve would be smaller, in the range £450 million to £600 million, say £500 million, with the underspend being correspondingly smaller.

5. Since this costing was made in 1980, departments have gained greater expertise in living within cash limits. So the estimated costs given above may be on the high side, the cost might be a third less than the estimates given above ie about £300 million in 1982-83 prices, so the effect on the Contingency Reserve would be between £300 million and £450 million, depending on when the debits for carry-forward are made.

ANNEX 2: EXISTING END YEAR FLEXIBILITY SCHEMES

The only case where a department is allowed to carry over expenditure is the overseas aid programme. Most of this programme is cash limited, but there is a proportion which consists of non-voted expenditure not subject to cash limits. Under a long-standing arrangement, an underspend of up to £15million (about 1.5 per cent of the total) may be carried forward to be added to the aid programme in the next year but one, subject to Treasury consent. Similarly, any overspend is carried forward and deducted from the next year but one. In practice, these arrangements are held in reserve. ODA is expected to make all possible efforts not to overspend its programme. In particular, the roll-over provisions do not give ODA any excuse for breaching its cash limits.

2. Since 1981-82, nationalised industries have been allowed increases in short term borrowing from the NLF at the end of the year in excess of that year's EFL, within one per cent of forecast turnover and fixed investment expenditure and on condition that the amount of the excess is deducted from the following year's EFL. Maintaining the discipline for carry-forward of overspends depends on the additional cash not being available until the following year's EFL has been set. Thus the EFLs are set during the third quarter and the carry-forward scheme is only available in the final quarter. To date there is little practical experience of the scheme's operation.

3. Flexibility schemes exist within programmes. For example, within the framework of an overall cash limit which is subject to the same discipline as any other cash limit, the DHSS have for some years allowed individual regional health authorities to carry over underspending of up to 1 per cent of their revenue allocations into the subsequent year. Any overspending is deducted from its allocation in the next year. Health authorities are also allowed to carry over underspending of up to 10 per cent of their capital expenditure allocation, with the adjustment being made in the next year but one. They also have some freedom to shift resources between capital and current expenditure. These arrangements appear to have worked well for several years. DHSS believe that the arrangements for revenue carry-over, while not eliminating underspending, have enabled them to reduce it below what it would otherwise have been and that it also helps to reduce wasteful expenditure at the end of the year.

4. An analogous arrangement has been introduced with effect from 1981-82 for local authorities' capital expenditure. Within a national cash limit for the bulk of local authority capital expenditure, individual authorities may carry forward an unspent allocation up to 10 per cent of the total to a subsequent year, anticipate a subsequent years' allocation by the same amount, or both. Other features of the scheme give further flexibility. It is too early to judge whether the scheme is compatible with maintenance of strict control on the national cash limit.

ANNEX 3: THE ROAD PROGRAMME

Note by the Department of Transport

This note sets out the particular problems in the application of an annual cash limit to the Roads etc. England vote. These arise from the problems of reconciling expenditure on the roads programme which comprises about 98 per cent of the Vote, and in the short run is inherently volatile, with an inflexible annual limit.

2. About three-quarters of the vote is for new construction and improvement schemes, including preparation and supervision. Two-thirds of the rest is on structural maintenance, which although classed as current expenditure is akin to capital expenditure. Road construction is necessarily a long-lead programme. Schemes making up the programme commonly take four years to complete with most of the expenditure concentrated in the second and third years. Up to 90 per cent of prospective expenditure in any individual financial year is committed before the year starts, and most of the rest is generally committed in the first half of the year. The scope for adjusting cash flow to meet fluctuations during the year in which they occur is therefore limited. As the rest of the cash block is small, it gives no significant scope for balancing uncontrollable deviations in the main programme.

3. Problems first arise because the indices used to establish the cash limit for the vote are extremely volatile. Assumptions made when the cash plans are agreed can be overtaken even before the year begins, as was the case this year (1982-83). Not only are future trends unpredictable, but partly because of problems of analysis, reliable information on past movements is not available until up to a year after the event. The interdepartmental Working Group on Roads Revaluation set up in 1981 found no way of remedying this situation. Without a reliable method of predicting price movements, the Department must therefore plan against a background of considerable uncertainty.

4. Various factors add to the uncertainties. As with other construction programmes, when the construction industry is short of work, tenders can be particularly keen. If, on the other hand, contractors are in a stronger position, tenders may be higher than expected. The road construction industry moreover is specially vulnerable to certain cost changes: the cost of oil, for example, affects the cost of bituminous surfacing as well as transport costs and those of operating plant on site. These are substantial elements in their costs. The industry's annual wage settlement generally takes place in July. This is early enough in the financial year significantly to disturb costs if an unexpectedly high increase is agreed, but too late to allow significant changes to commitments for the year.

5. The Department constantly refines its techniques for predicting the pattern of payment on contracts and relating these to commitments. There remains, however, a substantial random element which can cause major deviations from the projections on any one scheme.

6. The weather is a major cause of these random changes. Large-scale road building entails moving large volumes of earth, in some cases to clear the way for a road, in nearly all cases to use after compaction as the base for the carriageway. Weather conditions will have a marked effect on such operations, and can cause substantial variations in spending. Other operations are delayed by unseasonably cold weather. In unusually favourable conditions contractors can improve on expected progress and become entitled to larger progress payments than forecast. In poor conditions work can be delayed, even brought to a halt, and the projected scale of payments then becomes an overestimate.

7. Another uncertainty arises from the timing of claims arising from variations in contract or unforeseeable difficulties of terrain. Sometimes contractors are unpredictably slow in submitting claims: at other times, claims are prompt or applications are made for them to be made more frequently than is usual. Problems can also arise with the programming of large construction schemes where local or even national opposition can cause postponement at short notice. This can radically alter prospects in a very short time and, if it occurs well into the year, there is no prospect of offsetting delays by adjusting the programme. Large schemes especially cannot be replaced or rescheduled quickly.

8. Within the constraint of an inflexible annual cash limit, the Department cannot run the risk of deliberately aiming high in its plans, because it could not accommodate the possibility of an overspend. The scope for then using up the headroom later in the year should it not be required is however very restricted: contracts cannot be released to reduce it as they would not generate significant expenditure in time - and they would tend to over-commit the programme for the following year.

9. Flexibility between years would provide a way of smoothing out the effect of all these unpredictable short-run variations in the cost and rate of road building and thus improve the efficiency of management of the programme.

ANNEX 4: EXAMPLE OF HOW END YEAR FLEXIBILITY SCHEME MIGHT OPERATE

The following simple example illustrates how the scheme might work. The essential features are carry-forward of underspending up to a maximum, starting in 1982-83, but with no credit allowed for underspending in 1981-82. The scheme is compared with the situation where there is no end year flexibility ie the "do nothing" situation. In the example "surge" is used as shorthand to describe low priority expenditure which may be brought forward at the end of the year to reduce underspending on a cash limit. The numbers in the example are merely illustrative and are not intended to show the possible cost of the scheme.

£million

	1982-83	1983-84	1984-85
A. Do nothing			
Provision	1000	1000	1000
Expenditure	990	990	990
Shortfall	10	10	10
B. End year flexibility			
Basic provision	1000	1000	1000
Augmented provision	1000	1020	1020
Normal shortfall	10	20	10
Lack of surge	10		
Expenditure	980	1000	1010
Total underspend = carry forward	20	20	10
Cost of scheme			
ie additional expenditure compared to do nothing situation.	-10	+10	+20

2. In 1982-83, the exmaple assumes that total underspend is £10m more than in the "do nothing" situation. This is attributed to the lack of end year surge, as the department knows that it can transfer its underspending to 1983-84. The cost in 1982-83 is therefore -£10m.

3. In 1983-84, the example assumes that actual spending is £1000m, and that carry-forward to 1984-85 exactly balances what was brought forward from 1982-83, at £20m. The cost of the scheme is therefore £10m, the amount of the normal shortfall. In

principle, there would be no need for the department to claim on the contingency reserve, since its actual spending equals its basic provision. But in practice, the department might think part way through the year that it will spend the £20m it had brought forward from 1982-83, and claim it from the reserve. In this case the £10m costs of the scheme would be made up of £20m from the reserve offset by an additional £10m underspend (£20m instead of £10m in the "do nothing" situation).

4. In 1984-85, the example assumes that actual spending is £1010m, ie that carry-forward to 1985-86 is £10m less than the underspend brought forward from 1983-84. The cost of the scheme is therefore £20m. Again, the department might claim the full £20m from the reserve part way through the year; in this case the £20m cost exactly matches the drawing from the reserve, because total underspend is the same as in the "do nothing" situation.

5. The example shows that the cost of the scheme in any one year (after 1982-83) depends on two elements.

(i) the amount of normal shortfall without flexibility

(ii) the balance between the amount of underspend brought forward, and the amount carried forward.

The second element can be positive or negative, and might be expected to balance out over time. The two elements are not independent, however: if a department plans to use up all the underspend it has brought forward from the previous year, it will probably not be able to eliminate all its normal shortfall, as the augmented provision will act as an absolute constraint in the same way as cash limits in the current system.

6. An optional feature of the scheme might be that any second year carry-forward would not be automatic, but would be reserved for Ministrial discussion and agreement. In the example, in 1983-84, there would be no automatic carry-forward of £20m to 1984-85, since actual spending matches basic provision. This £20m carry-forward would be reviewed before being added to the basic provision for 1984-85.

ANNEX 5: HOW A 'VOTED' FLEXIBILITY SCHEME MIGHT OPERATE IN MOD

Note by the MOD

The capital etc. expenditures and receipts which are difficult to estimate and control with precision are spread throughout MOD cash limited votes. Subheads covering expenditures of about £7,500m and receipts of nearly £1,200m might be included within a flexibility scheme.

2. On the assumption that expenditure would in normal circumstances be evenly spread throughout the year, a 14 month year would allow about £500m of funds to be moved in either direction across the 31 March barrier. As far as MOD is concerned this would not have produced any increase in total expenditure over the last 5 years, because outturn has been very close to the cash limit over that period. The practical problem is that when a trend to either overspending or underspending is identified there is inadequate time to take smooth corrective action to the programme in-year, and the knock-on effect of such corrective action in future years needs to be taken into account.

Illustration A. Overspending.

Assume a continuing annual budget of £1,200m ie £100m per month.

By end-July the trend is 10 per cent too high. There is a 3 month lag in payments. Hence, action cannot effectively influence cash flow before end-October. By that time expenditure = £770m, leaving £430m to be spent in the remaining 5 months. Effective corrective action within the year would imply monthly expenditure by March running at about £80m ie well below the monthly level required for the following year.

If an overspend of up to £100m were permissible, it would be possible to limit the reduction of average monthly expenditure in the last five months of the year to a level consistent with a budget of about £1,100m in the subject year. If restraint were too effective the underspend facility would operate at the end of the second year.

Illustration B. Underspending.

Again, assume a budget of £1,200m ie £100m per month. By end-July the trend is 10 per cent too low. By end-October, total expenditure = £630m leaving £570m to be spent in 5 months. Effective corrective action within year would imply a level of monthly expenditure in excess of £120m by March, with consequent problems in following year.

If the facility existed to carry forward £100m, a long term monthly expenditure rate of about £100m could be arrived at ie consistent with a budget of £1,300m, in the second year.

If the expansion were overdone, the overspend facility would operate at the end of the second year.

3. The defence cash limit is treated in practice as a single, overall cash limit. If flexibility is to be limited to defined categories of capital expenditure, there might need to be some modification of this concept. The question of virement between subheads would also need to be examined.

4. An important feature of this scheme is that overspends and underspends would be carried forward automatically. This would facilitate the delegation of authority and responsibility for cash flow to managers without the fear that this would inevitably create large underspending. Taut estimating necessarily involves a symmetrical risk of overspending/underspending.

5. Under a 'voted' flexibility scheme it would perhaps not be necessary to surrender excess receipts at 31 March (as cfers).

6. Current accounting procedures might be reviewed. At present a great deal of attention is directed to determining the exact sums to be booked to vote in a particular year and long after a year has ended there is uncertainty, within £50m in either direction, what the total will be. Precision may be less necessary if succeeding financial years overlapped.

2 JUL 1982

CONFIDENTIAL

cc JV
Econ Pol

Prime Minister (2)

MCS 29/6

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

PRIME MINISTER

MONITORING REPORT: PUBLIC TRADING SECTOR

..... I attach the latest monitoring report on the public trading sector.

2. The British Rail and London Transport rail situation is of course being dealt with separately. Apart from that, the power engineers in the electricity industry have settled for 7.4 per cent on earnings, which is the same as the earlier manuals' settlement mentioned in the last report; and the British Transport Docks Board seem near to a 6 per cent settlement, which is not unhelpful.

3. As you will have seen from the correspondence resting with Nigel Lawson's letter to me of 24 June, the arbitration award for the gas manuals differed from the employers' 7.9 per cent offer only by a limited consolidation of bonuses, worth no more than 0.4 per cent and probably less. This is satisfactory as far as it goes, though the offer was a high one. But as I said in my letter of 14 June, I do not think that this detracts from the desirability of getting unilateral access to arbitration removed, here as elsewhere. E Committee decided last November that this should not be pursued with British Gas because of the sensitivities which Nigel mentions, and I accept that these still remain. But I do not on that account regard the position as unchanged since November: at that time the arbitration arrangements had been very little used, whereas now they have provided the basis for the latest pay settlement. I would hope that Nigel would be prepared at least to raise the matter with British Gas: we should not assume that it will become a further point of contention with them until we have their reaction.

4. In submitting the last monitoring report, I referred to doubts about British Telecoms' 6 per cent estimate of the cost of their main pay settlement (with their engineers). The present report records that they now put its value at 8.6 per cent, with a possible extra 1.3 per cent later in the year from restructuring. This can only reinforce the dissatisfaction which we have already expressed not only with British Telecoms' approach to these negotiations, but with their failure to keep us properly in the picture. We will need to ensure that they do better in the coming year.

5. I also referred to reports of pressure from water service manuals for a special 15 per cent comparability increase, and Tom King has responded in his letter of 21 June. It is disturbing that this is expected to be subsumed in the annual pay negotiations in the autumn. It could lead to pressure for a damagingly high settlement which the National Water Council, in its last major pay negotiation, would fail to resist adequately. I think we need to consider seriously now whether there is anything we can do to put a brake on those negotiations, perhaps by getting the Regional Water Authorities to take a closer interest. Perhaps Tom King could let me know what options we have.

6. Finally, the National Girobank are offering a 6 per cent increase plus a productivity scheme which will add another 3 per cent. I understand that the intention is to make payments under the scheme only as productivity savings actually accrue, and only to the value of half the savings achieved. I hope that Patrick Jenkin will be able to find ways of monitoring performance in a way that enables the progress of this scheme to be checked, so that it does not automatically give the staff what is in total a large increase.

7. I am copying this minute to the Home Secretary, The Secretaries of State for the Environment, Industry, Trade, Transport, Energy, and Employment, and to Sir Robert Armstrong and Mr Sparrow.

(G.H.)

29 June 1982

CONFIDENTIAL

PUBLIC TRADING SECTOR

PART 1 CURRENT AND FORTHCOMING NEGOTIATIONS

A. 1981/82 PAY ROUND

1 Electricity Supply: Power Engineers (29,300)
Settlement date: 1 February
Unions: EPEA/EMA

The union submitted an uncosted claim in January which included the preservation of links with industrial scales, the restoration of 1975 differentials and other improvements. The Electricity Council made an offer of 7% on basic rates at a National Joint Board meeting on 15 June. The offer was rejected and further discussions took place on 18 June when a settlement was reached which gave engineers an increase of 7.3% on the first 9 salary points increasing to 7.6% at the top point. The effect is to increase average earnings by 7.4%, and the annual pay bill by 7.2%.

2 Electricity Supply: Clericals - 47,000
Settlement date: 1 May
Union: NALGO

The group traditionally await the outcome of the manuals' settlement, which was concluded at the end of May and is worth 7.4% on earnings.

3 British Rail: Clerical and Conciliation grades (150,000)
Settlement date: 20 April
Unions: NUR, ASLEF, TSSA

British Rail have offered a 5% increase on basic rates from 6 September (not backdated to the April annual settlement date). The offer is conditional upon the unions agreement to accept, by 30 July, those productivity issues (including ASLEF's acceptance of flexible rostering) which are still outstanding from the 1980/81 pay round.

The offer has been rejected by the NUR, ASLEF and TSSA.

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ASLEF have reaffirmed their intention to take industrial action if the British Railways Board attempts to impose flexible rostering. The NUR have announced an all out strike from 28 June against the Board's 5% offer and the fact that it is inextricably linked to productivity which the union considers unacceptable. At a meeting of the Railway Staff National Council on 22 June, the Board put forward various ways in which the outstanding productivity items might be introduced, but the discussion was inconclusive. The Board are to put their proposals in writing for further union consideration.

Comment: Nothing has happened to lessen the likelihood of the all out strike threatened by the NUR taking place from 28 June.

Ministers have had full and seperate briefing on the current BR issues.

4 London Transport - Rail

(a) Railway Supervisory, Booking Office and Conciliation Grades (18,000)

Settlement date: 19 April

Unions: ASLEF, NUR, TSSA

The unions have submitted an uncosted claim for a substantial pay increase and shorter hours in line with the main British Rail claim. At a meeting on 7 April, management offered an increase of 5% on basic rates (expected to be worth 5% on average earnings also). In addition, management undertook to:-

(a) review relativities

(b) consider the case for an extra day's holiday (giving parity with bus staff)

(c) reduce working hours from 39 to 38 per week, as long as this could be done at negligible cost

(d) pay lump sum bonus worth in total half of any undershoot of the 1982/83 budget.

A meeting on 10 June resulted in little progress being made; ASLEF are against any proposed attempt to link pay to productivity. On 16 June LT offered to increase the existing 5% offer by an additional 1 or 2% in return for productivity improvements. LT hope negotiations will resume shortly.

Comment: The "flexible rostering dispute" between British Rail and ASLEF and the threat of industrial action by the NUR could have repercussions for London Transport; a call for action by the unions could receive a sympathetic response from members employed by LTE in the current climate of proposed reductions in services and manning levels. More immediately, there has been widespread industrial action following the implementation of new Underground timetables from 21 June. LT have offered the unions a peace formula which entails setting up a working party to find another way of achieving the economies, with the proviso that if no solution is found within 2 weeks the unions will have to accept implementation of new schedules. The NUR executive meet on 24 June to consider the dispute, and could follow ASLEF in calling indefinite action.

(b) Rail Workshop grades(3,550)

Settlement date: 22 April

Unions: ASBSBSW, AUEW, EEPTU, FTATU, NSMM, NUSMWCHDE, TGWU, UCATT, NUR

At a meeting on 20 April management offered a 5% increase on basic rates (worth around 5% on average earnings also) which the unions are considering. No further negotiating meetings have so far been arranged.

5 London Transport - Buses

(a) Bus Platform Staff (19,800)

Settlement date: 28 March

Union: TGWU

In response to an uncosted claim for substantial increases to basic rates and for the consolidation into basic entitlement of 4 days holiday currently associated with Bank Holidays, management offered increases worth 7% on average earnings (of which 0.5% would come from a self financing productivity scheme) and consolidation of the 4 days holiday into basic entitlement.

Although recommended for acceptance to a union delegate conference which took place on 3 June, conference decided to refer the offer to Branch Committees, who are believed by LT to have rejected it, though they have yet to hear officially. No further meetings have been arranged.

(b) Road Operating Supervisory grades - 2,500

Settlement date: 28 March

Union: TGWU

Negotiations traditionally follow those of the bus platform staff.

(c) Road Workshop Wages grades - 3,300

Settlement date: 22 April

Unions: ASBSBSW, AUEW, EETPU, FTATU, NSMM, NUSMWCHDE, TGWU, UCATT

Management will shortly make two written offers; either 5% on basic rates or a higher percentage if improvements to productivity can be agreed.

6 West Yorkshire Passenger Transport Executive: Platform Staff - 2,751

Settlement date: 1 May

Union: TGWU

A ballot of the membership by the TGWU rejected the PTE's offer worth 6.9% on average earnings plus a self financing attendance bonus and supported a call for strike action. Further negotiation has resulted in management withdrawing a proposal for a change in working practices to allow greater flexibility and there has been a second ballot on the offer. The result, announced on 18 June, failed to produce a conclusive result. A further ballot was being held on 24 June.

7 British Transport Docks Board: manual grades - 3,120

Settlement date 22 April

Unions: NUR, CSEU, EETPU, UCATT, TGWU

Management have improved their offer of 5% on rates to 7% on basic rates, an increase of 2.2% on the bonus and overtime calculators and 2 additional days holiday (in line with Registered Dock Workers). The effect of the offer on average earnings will be 6% and it has been recommended for acceptance by the Executive Committees. Formal acceptance has been received from the NUR and is awaited from the CSEU and the other minor unions.

8 Gas Supply: Staff and Senior Officers - 57,700

Settlement date: 1 June

Unions: NJC - NALGO, MATSA

BGC made an offer worth just over 6% on average earnings at a meeting on 17 June. The offer comprises increases ranging from 5.5% for those in the lower grades to 7.0% for the middle and higher grades. The unions said that the offer was unacceptable. No further meeting has been arranged.

Comment: The recent arbitration award for gas supply manuals worth 7.9% on average earnings in a full year (see item 15) will influence negotiations. Any settlement will in turn influence negotiations with the Higher Management Group (3,600 SD: 1 June) who have submitted an uncosted claim which includes increases of 12%, restoration of differentials over staff and senior offices and grade restructuring. The higher management have already rejected an offer of 6% on salaries, and negotiations are to be resumed on 24 June.

9 Water Service: Staff - 35,300
Settlement date: 1 July
Unions NALGO, GMWU, NUPE, GLCSA, TWSA

An uncosted claim for an increase in line with the RPI, a 1 hour reduction in the working week (to 36 hours) and 1 additional day's holiday was submitted on 22 April. On 21 May management offered 6.5% across the board (worth 6.5% on average earning s also) which was rejected. At a meeting on 10 June, management improved their offer to 7% on salaries and marginally increased holiday entitlement. The offer was rejected at NALGO's annual water staff group meeting on 14 June. That meeting instructed the National Water Committee to obtain an improved offer or prepare a programme of industrial action. At a further meeting of the Standing Joint Committee on 22 June the employers did not improve their offer. The unions are now deciding what action to take. No further meeting has been arranged. Indications are that initially any action will be rather low key, including withdrawal of cooperation from planned reorganisations.
Comment: Negotiations are influenced by the manuals' settlement effective from December 1981 when increases worth 8.8% on average earnings were awarded. Staff consider the restoration of differentials to be a main issue in their claim. The Water Combined Employer's Committee have advised their negotiators that an offer of up to 7½% may be made.

10 Water Service: Manuals - 30,000
Settlement date: 7 December
Unions: GMWU, NUPE, TGWU, NUAAW

The 1981/82 pay settlement (effective from 7 December 1981) included the setting up of a working party to review the wages of water service manuals in relation to manual workers in the economy generally. The NWC indicated to DOE officials at the time that they envisaged the review being a long term exercise and informal joint discussions have taken place. Press reports arising from

statements at the recent GMWU conference indicate the union's intention to seek a 15% increase in earnings to be paid before the annual settlement date. The employer's current concern is with improvements in performance and it is the NWC's view that there are unlikely to be any substantive developments in advance of the annual pay negotiations.

11 British Nuclear Fuels Ltd: Industrials - 9,190

Settlement date: 1 July

Unions: GMWU, AUEW, TGWU, EETPU

An offer of 7½% on earnings in line with the staff settlement has been made. At a meeting on 16 June, management refused to increase the offer, and the unions are now consulting their members. Management believe that acceptance is likely.

12 Post Office and National Girobank

(a) Postal Supervisors, Executives and Supervisory Catering grades - 14,800

Settlement date: 1 April

Union: CMA

The Post Office has yet to make an offer. The CMA is unlikely to accept increases less than those recently awarded to members of the UCW (7.6% on average earnings).

(b) National Girobank Clerical, Typing, Secretarial and Data Processing grades - 5,200

Settlement date: 1 July

Union: CPSA, SCPS

Management are to offer a 6% increase in salaries and a productivity scheme which, it is estimated, will provide a further 3% on earnings. No further information is available at present.

13 British Telecom

(a) Radio Officers, Telephonists, Telegraphists - 36,000

Settlement date: 1 July

Union : UCW

A 6.25% increase on rates is under discussion. The union are pressing for a 7% offer in line with the Post Office UCW settlement. British Telecom are resisting a higher offer.

(b) Clerical, Typing, Secretarial and Data Processing grades - 35,000

Union: CPSA

(c) HCO, EO, HEO, Welfare, Information grades etc - 6,300

Union: SCPS

(d) Telephone, Telegraph and Radio Supervisors - 6,000

Unions: CMA

5.2% offers to each of (b) (c) and (d) above are under discussion.

14 British Airways: All grades (excluding pilots) - 40,000

Normal Settlement date: 1 January

Unions: TGWU, AUEW, EETPU, NUSMU, APEX, FTATU, GMWU, UCATT, ACTSS, ASTMS, MNAOA

On 10 September 1981, British Airways announced a "rescue plan" aimed at stemming large financial losses. The plan included a reduction of 9000 jobs by June 1982, the reorganisation of many working practices and a pay freeze at least until 1 October 1982.

For the purpose of negotiation on pay and conditions of employment, staff are divided into 11 functional groups called National Sectional Panels on which all unions are represented. Although postponement of the annual settlement was accepted, 3 panels (Engineering and Maintenance, Ramp and Ground Service Staff) submitted claims for substantial increases although there was no immediate pressure to open negotiations.

Staff in the Engineering and Ground Service groups employed at Terminal 3 have pressed hard for a 1982 pay increase to take effect before 1 October. Lightning stoppages have been called off after management's agreement to commence pay talks on 5 July. Whilst no percentage figures are being mentioned at this stage, management intends not to allow any advancement of the date of any increase to raise the cost of the award during the pay year.

Comment: Although management are opening negotiations on 5 July only with the Engineering and Maintenance groups, any subsequent settlement will set the tone for all other future negotiations.

PART 2

SETTLEMENTS CONCLUDED SINCE THE LAST REPORT

15 Gas Supply: Manuals - 41,300
Settlement date: 17 January
Union: GMWU, TGWU

An arbitration award, which is binding on both sides, was made on 4 June and comprised the following:

(a) increases in basic rates ranging from 7.5% for labourers to 8% for technicians with full flow through into bonus payments;

(b) an increase of 50p per week in the General Obligations Payment (for flexible working procedures);

(c) an increase of £2.50 a week in stagger payments (for working outside normal hours);

(d) improvements to the local holiday bonus supplement and a relaxation of the rules governing local holiday entitlement.

In addition, with effect from 1 January 1983, there will be an alteration of the earnings structure which will involve a minimum fall-back bonus of 7% and the introduction of a £2.50 per week incentive bonus for non-bonus employees.

The award is essentially the same as BGC offered to the unions on 10 March with the addition of earnings restructuring from 1 January 1983. The effect on average earnings has been estimated by BGC to be the same as the 10 March offer (7.6% in the first year; 7.9% in a full year). The cost of the earnings restructuring could add up to 0.4% to this.

16. British Telecom: Engineers , Technicians etc - 130,000
Union: POEU
Executive engineers, Inspectors, Technical grades - 22,500
Settlement date: 1 July
Union: SPOE

Both groups have accepted a 12 month settlement comprising a 6.75% increase on basic rates from 1 July (worth 6.9% on average earnings) and the consolidation of 1.25% of a previously committed productivity bonus from 1 January 1983.

Other minor improvements and the implementation of a consolidation commitment from the previous round (on 30 June 1982) will result in an increase in average earnings estimated by BT to amount to 8.6% in the first pay year. If BT implement proposals for some grade restructuring later in the year, the average earnings figure could be increased by a further 1.3%.

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ANNEX 1

PUBLIC SECTOR SETTLEMENT DATES IN THE NEXT FIVE MONTHS

SETTLEMENT DATE	NEGOTIATING GROUP
1 July 82	Civil Service - Industrials (147,000)
1 July 82	Local authority groups-Building and Civil Engineering (Scotland) (19,734)
1 July 82	Local authority groups - APT & C Grades (590,000)
1 July 82	GLC/ILEA - APT E & C Grades (19,000)
1 July 82	University groups - Clerical Consortium (19,000)
1 July 82	Bank of England Staff (4,430)
1 July 82	British Telecom - Radio Officers, Telephonists, Telegraphists (36,000)
1 July 82	British Telecom - Telephone, Telegraph and Radio Supervisors (6,000)
1 July 82	British Telecom - Clerical Typing and Secretarial Grades (35,000)
1 July 82	Water Service - Staff (35,300)
1 July 82	British Nuclear Fuels Ltd - Industrials (9,190)
1 September 1982	Police - ranks up to Chief Superintendent (118,520)
1 October 1982	United Kingdom Atomic Energy Authority - Manuals (4,760)
1 November 1982	Coalmining - Manuals (198,000), Clericals (13,600) Deputies (18,200)
1 November 1982	Greater Manchester Passenger Transport Executive - Platform Staff (5,595)
4 November 1982	Local authority groups - Manuals (1,077,000)
4 November 1982	Local authority groups - Building Trade Operatives (76,000)
4 November 1982	Local authority groups - Engineering Craftsmen (10,400)
4 November 1982	Local authority groups - Electricians (5,430)
7 November 1982	Fire services - ranks below Chief Officers (39,000)

ANNEX 2

KEY TO ABBREVIATIONS

ABS	Association of Broadcasting and Allied Staffs
ACTSS	Association of Clerical Technical and Scientific Staff
AMMA	Assistant Masters' and Mistresses' Association
APEX	Association of Professional, Executive, Clerical and Computer Staff
ASLEF	Associated Society of Locomotive Engineers and Firemen
ASBSBSW	Amalgamated Society of Boilermakers, Shipwrights, Blacksmiths and Structural Workers
ASTMS	Association of Supervisory, Technical and Management Staff
AUEW	Amalgamated Union of Engineering Workers
AUT	Association of University Teachers
BALPA	British Airline Pilots Association
BDA	British Dental Association
BESO	Bank of England Staff Organisation
BMA	British Medical Association
COHSE	Confederation of Health Service Employees
CMA	Communication Managers' Association
CPSA	Civil and Public Servants Association
CSEU	Confederation of Shipbuilding and Engineering Unions
EETPU	Electrical, Electronic, Telecommunication and Plumbing Union
EIS	Educational Institute of Scotland
EMA	Engineers' and Managers' Association
FTATU	Furniture, Timber and Allied Trades Union
GLCSA	Greater London Council Staff Association
GMWU	General and Municipal Workers Union
ISTC	Iron and Steel Trades Confederation
LACSAB	Local Authorities' Conditions of Service Advisory Board

MATSA	Managerial, Administrative, Technical and Supervisory Association
NAHT	National Association of Head Teachers
NALGO	National and Local Government Officers Association
NAPO	National Association of Probation Officers
NAS/UWT	National Association of Schoolmasters and the Union of Women Teachers
NATFHE	National Association of Teachers in Further and Higher Education
NATTKE	National Association of Theatrical, Television and Kine Employees
NCCC	National Craftsmen's Co-ordinating Committee
NSMM	National Society of Metal Mechanics
NUAAW	National Union of Agriculture and Allied Workers
NUB	National Union of Blastfurnacemen
NUJ	National Union of Journalists
NUM	National Union of Mineworkers
NUPE	National Union of Public Employees
NUR	National Union of Railwaymen
NUT	National Union of Teachers
NUSMWCHDE	National Union of Sheet Metal Workers, Coppersmiths, Heating and Domestic Engineers
PAT	Professional Association of Teachers
POEU	Post Office Engineering Union
RCN	Royal College of Nursing
SCPS	Society of Civil and Public Servants
SIMA	Steel Industry Management Association
SOGAT	Society of Graphical and Allied Trades
SORO	Society of Registration Officers
SPOE	Society of Post Office Executives
SSTA	Scottish Secondary Teachers Association
STAMP	Supervisory, Technical, Administrative, Managerial and Professional Section of UCATT
TGWU	Transport and General Workers Union
TSSA	Transport and Salaried Staffs Association
TWSA	Thames Water Staff Association
UCATT	Union of Construction, Allied Trades and Technicians
UCW	Union of Communication Workers
URTU	United Road Transport Union

File
Econ Pol

PRIME MINISTER

CABINET DISCUSSION ON PUBLIC EXPENDITURE

I have been asked to find half a day in September when you could discuss the above. There is a Cabinet on 9 September just after you get back from Scotland and another one on 30 September after your return from China and before the Party Conference.

As there will be quite a lot of people away on 9 September would you agree to have it on 30 September? It is proposed that there should be an all-day Cabinet with half of it taken up on public expenditure.

Agree?

CAROLINE STEPHENS

25 June 1982

Prime Minister (1) JV AW PA

Should I write round setting up this Cabinet meeting, indicating the need for discretion (it would be awkward if some of the options for consideration were publicly known in the autumn) and seeking co-operation for the CPRS work?

MCS 23/6

MCS 5/7

CONFIDENTIAL

Qa 05958

22 June 1982

To: MR SCHOLAR

From: JOHN SPARROW

Long-Term Public Expenditure

1. In his minute of 15 June (paragraph 17), the Chancellor suggests that the CPRS might provide a paper on long-term structural options, for the discussion he proposes of the officials' report on public expenditure prospects. I have now seen your reply of 21 June.

2. I agree that this is a job the CPRS ought to tackle, and I am glad that the Prime Minister has agreed. There is not much time before September, and as you know we have several other major reports to complete in the same time-scale. But for this first wide-ranging discussion, I take it Ministers will not want an elaborate paper with fully worked-out options. The object is not to reach firm decisions, but to have a preliminary debate on the broad options and then decide what further work should be set in hand.

3. There is one proviso. We shall of course need to consult the Treasury and draw on their thinking. But I think we must also be able to consult other Departments concerned. They are not likely to be enthusiastic contributors, but we must at least try out our ideas on them, to correct avoidable mistakes and prevent any accusation that we have circulated an important paper without giving them a chance to comment. No doubt we can arrange this when Departments have been informed of the Prime Minister's intention to call a meeting in September on the LTPE report, with an input from the CPRS.

4. There will inevitably be some slight risk of leaks in sensitive areas (charging for "welfare" services, pensions indexation, defence),

but in my view this risk (which we will of course do our best to eliminate) cannot be allowed to stop any exploration of options for Ministers.

5. I am sending copies of this minute to John Kerr (Treasury) and to Sir Robert Armstrong.

P.

PERSONAL AND CONFIDENTIAL

Econ Pol

PM

FILE

10 DOWNING STREET

From the Private Secretary

21 June, 1982

LONG TERM TRENDS IN PUBLIC EXPENDITURE

The Prime Minister read with interest the Chancellor's minute of 15 June, to which he attached a copy of the study by officials on the likely pattern of public expenditure over the next decade.

The Prime Minister is in agreement with the approach to these matters outlined in the Chancellor's minute. In particular, she agrees to an extended discussion with Cabinet colleagues in September (whether at Chequers or at No.10), and we will be in touch with you and the other Private Offices concerned to arrange a date. She agrees, too, that it will be useful to consider a CPRS paper on this subject at that time, and I would be grateful if John Sparrow would take this up.

I am sending a copy of this letter to Sir Robert Armstrong and John Sparrow.

M. C. SCHOLAR

John Kerr, Esq

HM Treasury

10 DOWNING STREET

Prime Minister

Long term Public Expenditure

3 papers

Flag A (1) The Chancellor's — pretty grim reading

Flag B (2) Alan Walters' & Ferdy Mount's comments

Flag C (3) Note from Robert Armstrong

Agree that there should be an extended discussion at Chequers in September? With a CPRS paper? Or No. 10 Yes Yes

Agree the Chancellor's general approach? Yes

MCS 18/6

Ref: A08717

PERSONAL AND CONFIDENTIAL

PRIME MINISTER

Public Expenditure in the Longer Term

In his minute to you of 15th June the Chancellor of the Exchequer has proposed that there should be a wide-ranging Cabinet discussion of public expenditure in the longer term, outside the framework of regular Cabinet meetings, that a half-day should be devoted to this in September, and that the meeting might consider three papers - the report by officials attached to the Chancellor's minute, a paper by the Chancellor himself and a paper by the CPRS.

2. There is a strong case on merits for a Cabinet discussion of public expenditure in the longer term. The danger is, as was recognised when the official study was put in hand on a low key basis, that difficult policy issues are bound to be exposed and, if the discussion leaks, there could be awkward presentational problems. Nevertheless you may think that, provided that reasonable precautions are taken, this risk should be accepted in the interests of developing realistic policies for the next Parliament.

3. On the proposed arrangements I am sure that it is right to have this discussion outside the framework of normal Cabinet meetings. A half-day discussion in a more relaxed environment, such as Chequers, at a time such as September, when Ministerial diaries are less crowded, seems appropriate. On the precise timing you will wish to consider in particular whether you agree with the Chancellor's judgment that it would be desirable to have the discussion before the Party Conference. If you decide on a half-day at Chequers you will want to give some thought to how such a gathering, whose existence will become publicly known, should be presented.

4. On the agenda I agree with the proposal that there should be a paper by the CPRS, and I understand that Mr. Sparrow is willing to take this on. He will be minuting you shortly on how he would propose to go about preparing the paper with the help of Departments.

PERSONAL AND CONFIDENTIAL

5. If you agree with the Chancellor's proposals, the next step would be to get a date reserved in Minister's diaries, with some clear understanding from the outset on how the occasion is to be presented. The timing will not be easy in view of the Chancellor's probable absence in the first half of September, your own provisional plans to visit China, Japan and Hong Kong in the period 18th-29th September, and the Party Conference. Perhaps Friday, 1st or Monday 4th October?

6. I am sending a copy of this minute to Mr. Sparrow.

RTA

Robert Armstrong

17th June 1982

B

cc Mr. Vereker

MR. SCHOLAR

LONG TERM TRENDS IN PUBLIC EXPENDITURE

1. We are sure it is right for the Chancellor to separate the broad strategy of public expenditure, over the next eight years or so, from the detailed discussion which will go on about next year's public expenditure. This is a much better structure to the discussion than the original proposal. Although, as John Vereker points out, it will be difficult in practice to separate it from immediate policy. Yet it is well worth a hard try.

2. Again the Chancellor is entirely right in his emphasis on cutting programmes. Only if the four major programmes are tackled will there be any real impact on spending. (This is the experience of the Reagan administration.) These involve major political decisions. One of the dominant issues must be the shift from public to private sector of social security, health and education. And although it would help, because of efficiency, to switch to private provision while maintaining public financing, the important step is towards private financing. With defence and police, of course, there is no possibility of private financing although there might be for additional private provision (through contracting out). ?

3. We agree with the Chancellor that there will need to be at least "a good half day". We suspect that there will need to be a follow-up discussion too.

4. On the desirability of stimulating discussion through a parallel study, some 12 months ago the Adam Smith Institute started a very wide-ranging and intensive study of public expenditure prospects. If it is successful, this will provide the review which the Chancellor is suggesting in paragraph 16. But it would be a good idea to encourage another study - perhaps through IEA or, more doubtfully, IFS to ensure appropriate coverage.

IEA

5. The report by the interdepartmental group of officials is itself a standing testimony to the need for new thinking on public expenditure. Left to itself, everything extrapolates at insupportable growth rates.

/6. Because

6. Because the Chancellor's study makes such grim reading, it presents an opportunity to shift the ground of the public expenditure argument in the direction of radical change. For two reasons, it could mark a turning point.

(a) The status quo looks less and less like a practical option for the next five years. It is no longer a question of "privatise to improve efficiency"; it is "privatise or the financial strain will bankrupt the Government".

(b) The study makes it clear that the shifting of nationalised industries into the private sector will not of itself alter the sums significantly. It is the great welfare departments - Health, Education and pensions - where substantial injections of private finance will be essential. In modern Western societies, these are all high-growth industries, and the state alone can no longer generate the income to support them.

FM

17 June 1982 FERDINAND MOUNT ALAN WALTERS

cc SV
AW

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

PRIME MINISTER

LONG TERM TRENDS IN PUBLIC EXPENDITURE

In my minute of 8 March, I suggested that officials should undertake an examination of the likely pattern of public expenditure over the next decade.

..... 2. This study has now been completed and I attach a copy of a report by a group of officials on which the main spending Departments, and the CPRS, were represented. The report considers what, on the basis of certain hypotheses about developments in the economy on the one hand and expenditure programmes on the other, public expenditure might amount to by 1990. Some of the hypotheses - for example about unemployment: see Annex 1 - are inevitably sensitive.

3. As expected, the picture is bad. Only on hypotheses that are rather favourable as regards the economy, and relatively modest as regards expenditure programmes, does public expenditure as a percentage of GDP come out lower in 1990-91 than it was in 1979-80. In cost terms the prospect on any of the hypotheses is for big increases over this period.

4. The report shows clearly how the balance of our public expenditure programmes has changed and will, on present policies, continue to do so. It also shows the extent to which the four largest programmes - social security, health, education and defence - dominate public expenditure. In 1979-80 the four programmes between them amounted to about 60 per cent of the total. By 1990-91, on these projections, they would amount to about 63½ per cent, even on the "best case". Within

that, defence would take a higher proportion and education a smaller proportion of the total.

5. The officials' report looks forward, and shows a generally rising trend of future expenditure. Forecasting in an uncertain world is difficult. But if we look backwards over the last twenty years (Table A annexed) a consistent upward pattern emerges, broken only by the two external crises of 1967 and 1976. Even then, the upward trend was soon resumed.

6. This pattern we need to break, decisively.

7. For this purpose, radical changes affecting most, if not all, of the major programmes will be required. They will need to be reinforced by action on the smaller programmes. But that in itself will not be sufficient. Unless we tackle major programmes in a fundamental way, I see no prospect of achieving our taxation objectives even in the next Parliament.

8. Originally I had in mind to circulate the officials' report for Cabinet discussion this month, so as to influence colleagues' approach to this year's Public Expenditure Survey Cabinet discussions. The latter are due to start on 15 July: we face a difficult prospect, as colleagues have put in numerous bids, some very large.

9. On reflection, however, I think it would be better if the report on long term public expenditure were to some extent distanced from operational decisions about the Survey, so that colleagues could be encouraged to see the report as providing the opportunity for a broad-ranging discussion about our long term objectives regarding public expenditure, and the size and shape of the public sector. This would pave the way for some major strategic decisions affecting our programmes as a Government for the next Parliament.

10. At the recent Versailles summit I was struck - just as I know you were - by the extent to which heads of government and finance ministers everywhere are confronted, like ourselves, by major problems of public expenditure, such as untenable commitments to indexation, and the large public sector deficits which represent a threat to economic recovery. This report can help us to convey some of these insights, even though it does not itself deal with international experience.

11. I think that it would be difficult to conduct a discussion of this kind within the framework of our regular Cabinet meetings. It seems to me that we need to put aside at least a good half-day for the kind of wide-ranging consideration of objectives that I have had in mind. If this were arranged in September, it could also form part of the preparation for this year's Party Conference, at which we shall no doubt be under pressure about various aspects of public expenditure. If you were attracted by the idea of proceeding in this way, I should of course circulate a paper of my own for discussion with the officials' report.

12. In it I would be looking for colleagues' endorsement of a number of important practical decisions as an essential preliminary to putting public expenditure onto a better track, and thus sustaining our economic strategy.

13. First, I would seek agreement to set work in hand on the scope for major structural changes in as many as possible of the four major programme areas. Smaller areas ought to be similarly examined if there is prima facie reason to believe that really significant reductions in expenditure could be made in them. A series of strategic reviews of this kind would be very different from the normal examination of options which is carried out during the public expenditure survey. They should not be inhibited by need for legislation, the existence of past commitments or the alleged political impossibility of change. There must be radical thinking. The aim should be

to produce a series of papers for Ministerial consideration, similarly no doubt in some special forum, no later than the spring of 1983. (The exercise would of course need to be handled on a restricted, and confidential, basis.)

14. I would also hope that colleagues would agree not to press for any new significant long term expenditure commitments, or the renewal of existing commitments. This will be important in the context of this year's Party Conference, where, as I said, we may come under pressure. I see this as essentially a holding operation, until we have been able to evaluate the strategic reviews, and assess the extent to which we shall in the light of them be able to make a really important impact on public expenditure.

15. There is also the matter of 1985-86. As I said, I hope that discussion of the longer term prospects can be to some extent distanced from this year's public expenditure operation. But we shall have to take decisions about the new year in the Survey, 1985-86. I hope that these decisions will reflect our determination to reduce public expenditure over the rest of the decade, and that colleagues will endorse a very cautious approach to expenditure in that year.

16. Lastly, there is the question how we can best educate public opinion in these matters. I believe it would help if we were able to find some way of arranging for an assessment of long term public expenditure prospects to be published by a non-governmental body, to provoke public debate and help to demonstrate the need for radical change.

17. If these ideas appeal to you, I hope that we might look to the CPRS for support in the form of a paper pointing up some of the long term options open to us, especially in relation to the kind of structural changes described in paragraph 13 above.

PERSONAL AND CONFIDENTIAL

18. I am sending copies of this minute to Sir Robert Armstrong and Mr. Sparrow only.

G.H.

15 June 1982

PUBLIC EXPENDITURE IN THE LONGER TERM

A report by an Inter-departmental group of officials

Introduction

This report considers the way in which the costs of the Government's public expenditure policies could develop over the rest of the decade, against the background of some assumptions about economic developments over this period.

2. The aim is not to forecast total public expenditure, or individual programmes, or the course of economic development. The public expenditure figures have been built up on the basis of the continuation of current policies at the programme level, and the economic scenarios have been constructed on specific assumptions. One should beware of any spurious sense of precision. The figures for individual programmes are not to be regarded as bids or targets, and the results cannot be other than very broad brush.

3. The report presents a snapshot of 1990. It also, in the notes on individual programmes in Annex 2, offers some comments on the path by which some of the programmes might achieve the levels shown for them in 1990. In general, however, it is not concerned with possible developments regarding public expenditure in the period between 1984-85 (the last year covered by Cmnd 8494) and 1990-91. But it is clear that if the Government intends significantly to influence the outcome as regards public expenditure in 1990-91, the necessary decisions would need to be taken a number of years in advance.

The Two Economic Scenarios

4. In considering the longer term implications of the Government's public expenditure stance, the report first adopts a set of assumptions about productivity, inflation, growth and unemployment which would represent a substantial and continuing improvement on our recent national economic performance. This is Scenario A. Its principal features are set out in Annex 1. The assumptions are that inflation will fall and remain at a modest level, that wage restraint, combined with lower tax rates and interest rates, permit

rapid rebuilding of profit margins, that productivity continues to grow well, and that economic growth will as a result be sustained at a level well above what has recently been achieved. Such a performance implies an all-round improvement in our affairs, and may not be far short of the best we can expect.

5. But things may not turn out like this. The UK has long suffered from low efficiency and poor productivity, and there is still much to do to improve the flexibility and performance of the economy. We are highly dependent on what happens in the world economy. The world economic environment remains very difficult. In common with our European neighbours, but to a greater extent than some of them, we have lost competitiveness, and despite some recent improvement will not easily regain it. It is accordingly necessary to look at public expenditure against the background of much less favourable economic assumptions than in Scenario A. In Scenario B, which is also described in Annex 1, the main differences from Scenario A relate to productivity growth (1½% instead of 3% per year in the decade of 1990), GDP growth (½-¾% instead of 2½%) and unemployment and inflation (which stick around their present levels instead of coming down).

6. None of this is to say that events will turn out precisely according to either of these scenarios. They are hypotheses, not forecasts; it would in particular be a mistake to suppose that a prediction of the future can be obtained by splitting the difference between them. But they seem to cover an adequate range of possibilities against which to examine public expenditure trends in the light of the Government's objectives.

7. These economic scenarios interact with public expenditure trends in two ways. On the one hand assumptions on economic growth, inflation, unemployment, interest rates, productivity and earnings growth are needed to cost the programmes. On the other hand the taxation and interest rate consequences of public expenditure have implications for the supply side of the economy and for employment and productivity. The presumption underlying Scenario A is that expansion of the private sector provides the main engine for growth in the economy and that this expansion would be promoted by reductions in taxation and interest rates and

hence in total public expenditure as a proportion of GDP.

The Public Expenditure Projections

8. In making the public expenditure projections it has been assumed that the Government will continue to constrain the size of the public sector by privatisation and restraint on expenditure. Firm intentions to privatise have been reflected in the expenditure figures, but no account has been taken of any substantial further privatisation. Allowance has been made for changes in expenditure as a result of demographic changes, and, for some economic services such as transport, for the likely growth in national income. But only limited allowance has been made for the likely increase, if national income grew as assumed in Scenario A, in the public's demand for some of the public services, notably health, education, and environmental services, and for increasing real social security benefits. (Social security benefits, for example, are assumed to increase by less than earnings). International evidence suggests that this demand could increase on a significant scale. The Government is not obliged to meet it and may decide to divert it into privately provided services. But the scope for such diversion is limited over this period. And local authority expenditure, although projected to continue its relative decline, may continue to be difficult to control.

9. The projections have been combined with the two economic scenarios to show what could happen to public expenditure as a proportion of GDP. This proportion is also a measure of the ratio of taxation and government borrowing to GDP; although to the extent that this is reduced by privatisation resources will not be released for expansion elsewhere. Privatisation of a corporation for example will move its borrowing from the public to the private sector, but this will not reduce interest rates.

10. The inflation assumptions in the two scenarios are very different, so it is not easy to interpret differences in expenditure between the scenarios when the figures are set out in current prices. The figures have therefore also been deflated by the inflation indices assumed in the two scenarios. This avoids measurement problems caused by changes in the value of money,

but takes account of changes in the relative costs of different elements in the various programmes. This means that the programmes, and the totals are expressed both in what are called "cost terms" and as a proportion of GDP.

11. The projections assume that levels of services over the period to 1990 will not, taking one year with another, be squeezed on account of inflation. The levels of service at which it would be appropriate for Ministers to aim if inflation were high is a matter for future decisions.

12. Figure 1 shows how, compared with 1979-80 and 1982-83, total public expenditure could develop on the basis of the two economic scenarios.

13. In cost terms, the 1990-91 programme total[1] in Scenario A is 20% higher than it was in 1979-80. In Scenario B it is 18% higher. As a percentage of GDP the total in Scenario A falls, compared with 1979-80, by a little over 1 percentage point, taking it back to where it stood in 1971-72. In Scenario B it increases by nearly 6 percentage points.

14. Comparison of 1990-91 with 1982-83 shows the programme total in cost terms at nearly 14% higher in Scenario A and 13% higher in Scenario B; as a percentage of GDP the total is nearly 4 points lower in Scenario A and 3 points higher in Scenario B. But this is in part because public expenditure in 1982-83 as a percentage of GDP has been increased by economic recession; this has reduced GDP and increased social security expenditure. It may therefore be a less satisfactory basis for comparison.

15. Figures 2 and 3 show how the various major programmes could contribute to these changes, expressed both as a proportion of GDP and in cost terms. In both scenarios the share of GDP devoted to

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[1] The term programme total is used here to describe total public expenditure as defined in Cmnd 8494 and previous public expenditure White Papers. Also shown in figure 1 is the wider total including debt interest and some other adjustments, often used for comparisons with GDP. The figures for 1979-80 are outturn and those for 1982-83 are Cmnd 8494 adjusted for the changes in public expenditure announced in the Budget.

defence would be higher in 1990-91 than in 1979-80; although with no non-pay relative price effect there would in Scenario A be no increase over 1982-83. Health and social security are shown as a broadly constant proportion in Scenario A, and a rising proportion in Scenario B. Education is shown as a declining proportion in both cases. The share of economic services (agriculture, industry, transport, nationalised industry borrowing), tends to fall, as does that of environmental services (housing, water and sewage, etc).

16. In cost terms, increases in major programmes from 1979-80 to 1990-91 on the basis of the assumptions in this report would be

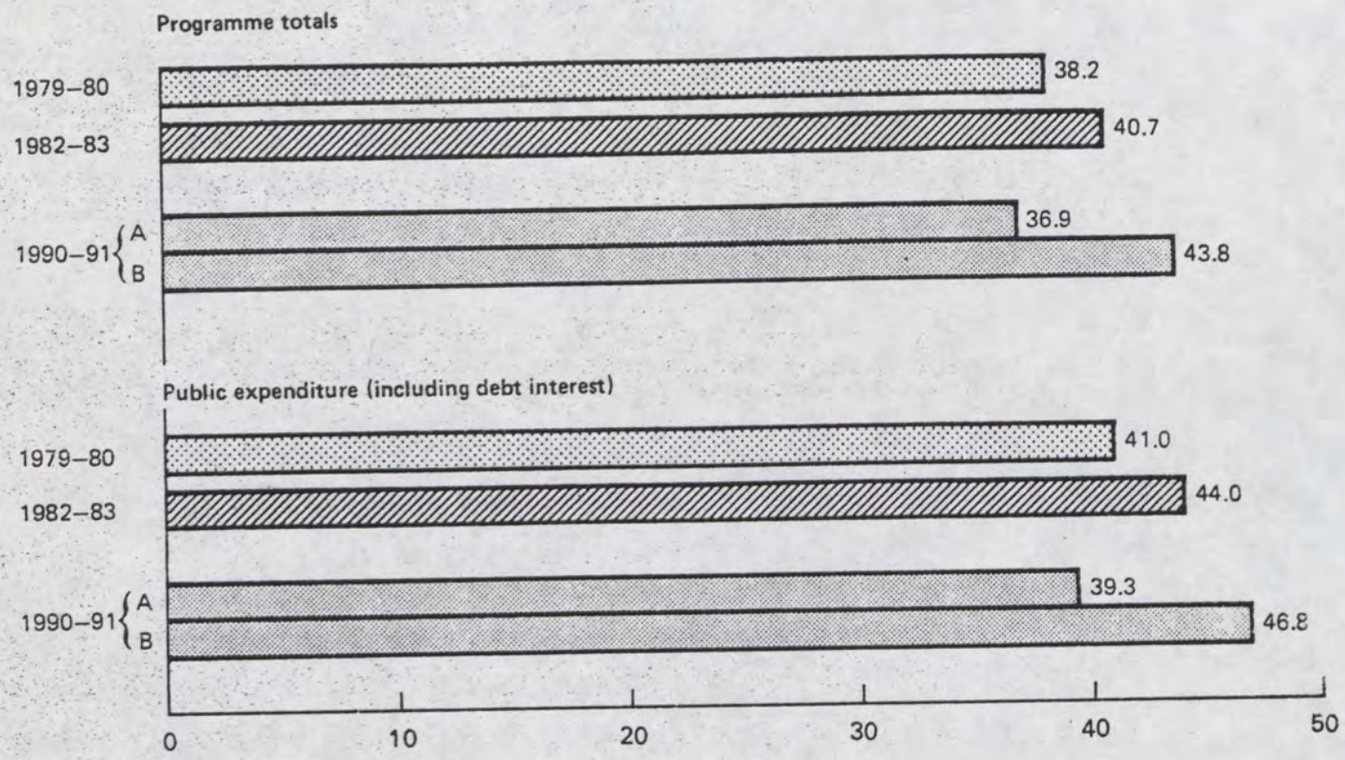
- 35 to 50 per cent in defence expenditure, depending in part on the assumed non-pay relative price effect
- 30 to 35 per cent in the law and order programmes
- 25 to 35 per cent in expenditure on health due largely to demographic pressures
- 20 to 25 per cent in the social security programme, even though demographic changes are relatively favourable for this programme in the 1980s, compared with the 1970s or the 1990s.

The cost of education would be slightly higher in Scenario A than Scenario B if economic growth increased the real earnings of teachers. Different economic situation could affect infrastructure and industry programmes; higher growth is taken, for example, to involve more road buildings; a sluggish economy could involve more assistance to industry and employment and housing expenditure.

FIGURE 1

Public expenditure

Percentage of GDP



£billion, 1980-81 cost terms

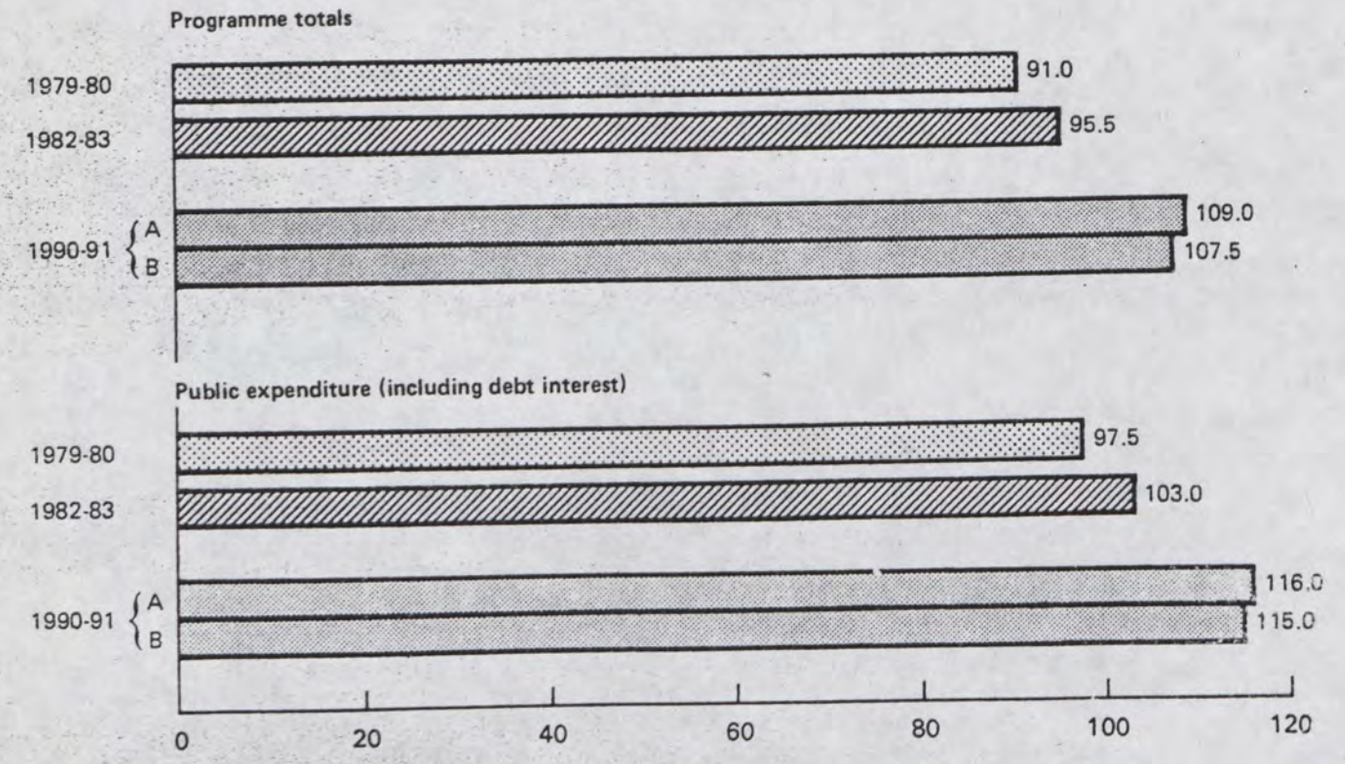
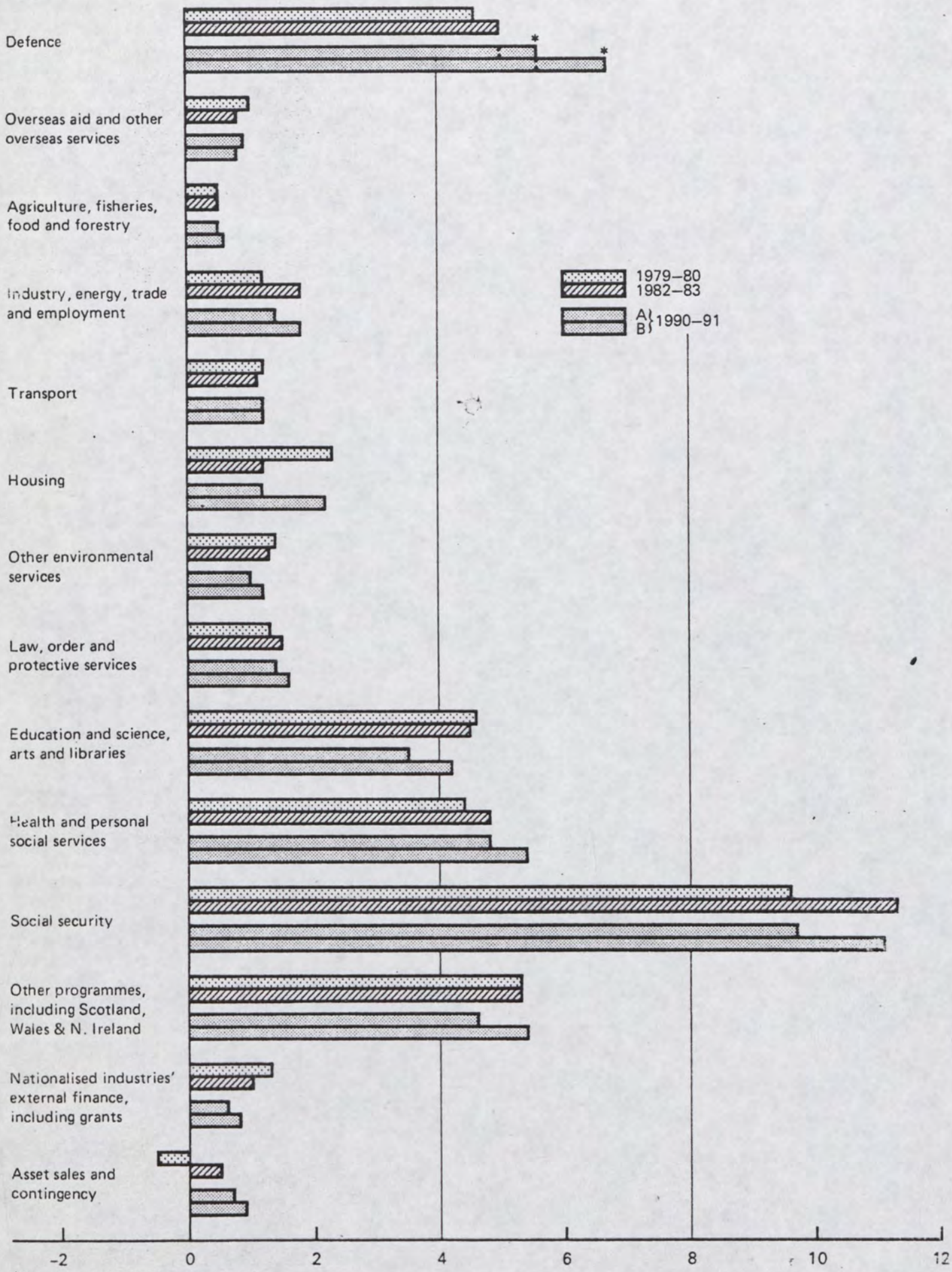


FIGURE 2 Public expenditure programmes

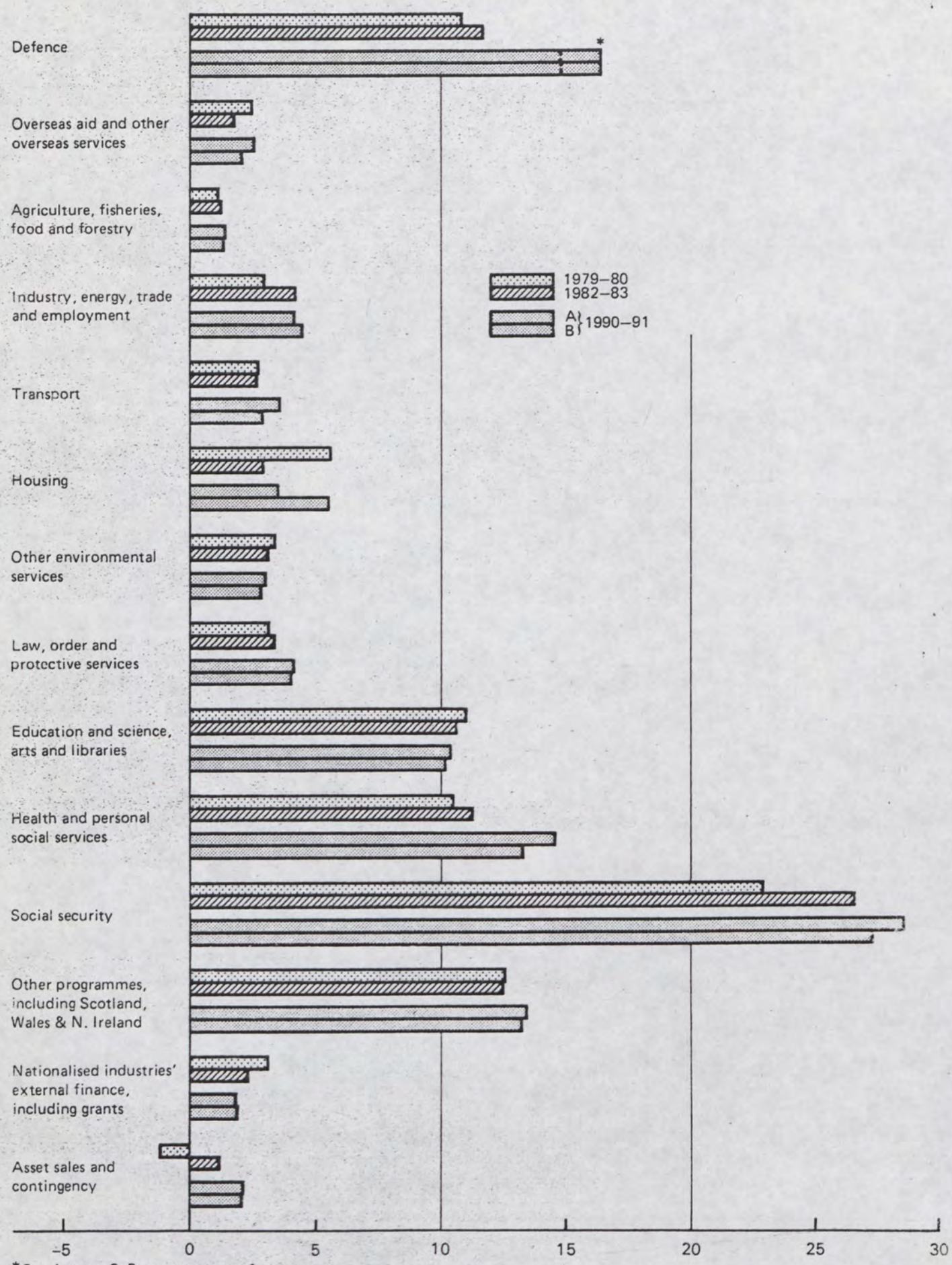
Percentage of GDP



*See Annexe 2, Programme note 1

FIGURE 3 Public expenditure programmes

£billion, 1980-81 cost terms



*See Annexe 2, Programme note 1

ANNEX 1

ECONOMIC SCENARIOS

The main assumptions of Scenarios A and B are summarised in Table 1. In Scenario A, economic growth in the 8 years to 1990-91 is similar to that of the 1950s and 1960s. In Scenario B growth is similar to that of the last 8 years. These growth rates are combined with the productivity assumptions and a small growth in the labour supply, to give consistent figures for unemployment.

2. Inflation is assumed to settle at 5% per year in Scenario A and 10% per year in Scenario B, although this has little direct effect on the public expenditure projections.

3. Scenario A assumes high productivity growth but, in the early years, much lower real wage growth. In Scenario B, real wages grow more rapidly than in Scenario A in the early years and more slowly in the later years. Public service wage growth is assumed in both scenarios to fall behind that in the marketed sector to 1982-83; thereafter wages in both sectors are assumed to grow at the same rate.

4. The change in public service wages relative to average GDP prices is a "relative price effect". This "pay-RPE" has been taken into account in projecting the public service expenditure programmes.

TABLE 1: ECONOMIC SCENARIOS - MAIN ASSUMPTIONS

	SCENARIO A	SCENARIO B
GDP (average annual growth rate from 1980-81)	2⅓%	¾% to 1985-86 then ⅓% to 1990-91
Productivity in the marketed sector (average annual growth rate from 1980-81)	3%	1½%
Unemployment (narrow definition, excluding school leavers)	2 million in 1990-91	3 million in 1990-91
Inflation (GDP deflator)	5% per year in mid and late 1980s	10% per year in mid and late 1980s
Real interest rate	2% in 1990-91	2% in 1990-91
Real trade-weighted exchange rate (1980-81 = 100)	83 in 1990-91	83 in 1990-91
Real marketed sector wages (average annual increase from 1980-81)	1½%	1½%
Real public service wages (average annual increase from 1980-81)	½%	¼%

ANNEX 2

EXPENDITURE PROGRAMMES

1. DEFENCE

1.1. The likely path of defence expenditure over the next decade is determined by the Government's commitment to the NATO target of 3 per cent annual real growth. At present this commitment does not extend beyond 1985-86. The UK supported the 1981 NATO Ministerial Guidance extending the Alliance's commitment to 1988.

1.2 In both scenarios, 3 per cent per year real growth is assumed, starting from the 1982-83 cost terms figure. It is assumed that the Government's commitment will be extended to the end of the NATO target period (1988-89) and there will be 1 per cent annual growth thereafter.

1.3. For the relative price effect (RPE) of non-pay expenditure alternative assumptions have been adopted of zero and 2 per cent positive from 1982-83. The effect of these assumptions on the projections for 1990-91 is shown in the table below.

TABLE 1.1. DEFENCE EXPENDITURE

	1979-80	1982-83	1990-91			
			A		B	
Non-pay RPE (increase per year) 1982-83 to 1990-91	-	-	0	2%	0	2%
£m (1980-81 cost terms)	10880	11732	14800	16400	14800	16400
% GDP	4.6	5.0	5.0	5.6	5.6	6.7

2. OVERSEAS AID AND OTHER OVERSEAS SERVICES

2.1 Like most developed countries we are committed to achieving a level of overseas aid of 0.7 per cent of GDP, but in general there is no commitment to a date. At present, the UK aid programme is fluctuating about 0.4 per cent of GDP, slightly above the OECD average. It is likely that cash expenditure on the aid programme will increase less rapidly than nominal GDP up to the mid-1980s.

2.2 The projections assume that in Scenario 'B', the aid programme will return to a level of 0.4 per cent of GDP by 1990-91. In Scenario 'A', some modest progress towards the 0.7 per cent target is assumed, reaching 0.5 per cent of GDP by 1990-91.

2.3 The other programmes for which the ODA is responsible (the aid administration vote; supplements etc to certain overseas pensions plus, from 1982-83 to 1984-85, foreign currency borrowing of £15m a year by the CDC) are de minimis in the context of this exercise, and are assumed to stay at roughly their present level in cost terms.

2.4 Other FCO expenditure will be affected to some degree by planned reductions in civil service expenditure and the general desire to achieve economies, although some of the expenditure (such as international subscriptions) cannot be unilaterally reduced. It has been assumed that this block of expenditure, and the small item covering the Commonwealth War Graves Commission, will remain broadly constant after allowing for inflation worldwide and exchange rate fluctuations.

TABLE 2.1 EXPENDITURE ON OVERSEAS AID AND OTHER OVERSEAS SERVICES, EXCLUDING NET PAYMENTS TO EC INSTITUTIONS

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 Cost terms)	1470	1363	2020	1510
% GDP	0.6	0.6	0.7	0.6

2.5 Net contributions to the European Community Budget are currently much lower than they would have been but for the refunds negotiated under the 30 May Agreement. That Agreement also commits the Community to avoid the recurrence of unacceptable budget situations for any member state. There will be strong pressure operating during the 1980's which will tend to increase the UK's net contributions before refunds: the growing costs of supporting farm incomes and disposing of surpluses this may produce, the extension of the Common Agricultural Policy to cover Mediterranean products and the accession of Spain and Portugal to the Communities. Maintenance of the ceiling on the Communities "own resources", under which they are entitled to the yield of a value-added tax not exceeding the 1 per cent of the value of transactions incorporated in the harmonised spending base, may help to contain EC expenditure on these policies. But a satisfactory outcome for the UK net contributions will depend on our success in persuading the Community to provide budget refunds on an acceptable scale.

TABLE 2.2 NET PAYMENTS TO EUROPEAN COMMUNITY INSTITUTIONS

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 Cost terms)	1010	415	500	500
% GDP	0.4	0.2	0.2	0.2

2.6 Aggregate expenditure on Programme 2 is summarised in Table 2.3

TABLE 2.3 TOTAL EXPENDITURE ON OVERSEAS AID AND OTHER OVERSEAS SERVICES

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 Cost terms)	2480	1778	2520	2010
% GDP	1.0	0.8	0.9	0.8

3. AGRICULTURAL, FISHERIES, FOOD AND FORESTRY

3.1 A large part of the expenditure covered by this programme is affected by the rules of the Common Agricultural Policy, for which both the future direction of policy and the basis for funding are very uncertain over the longer term.

3.2 The projections are based on the assumption that, apart from the completion of the Thames tidal defences, expenditure by MAFF increases at 1 per cent per year in cost terms from the level of the mid 1980's, as does Forestry Commission expenditure, while expenditure by the Intervention Board for Agricultural Produce increases at about 2 per cent per year throughout the decade. The projections exclude an allowance for capital expenditure by RWA's, as explained in para 8.2 (Other Environmental Services).

3.3 Main programme 3 includes some expenditure outside England, but teritorial programmes also include expenditures on agriculture. These are assumed to amount to £200m (1980-81 cost terms) in 1990-91 for both scenarious, ie similar to their relative size in 1980-81.

TABLE 3.1 EXPENDITURE ON AGRICULTURE, FISHERIES, FOOD AND FORESTRY

	1979-80	1982-83	1990-91	
			A	B
MAFF £ (1980-81 Cost terms) % GDP	650 0.3	577 0.2	520 0.2	510 0.2
IBAP £ (1980-81 Cost terms) %GDP	435 0.2	570 0.2	840 0.3	820 0.4
Forestry £ (1980-81 Cost terms) % GDP	55 -	53 -	50 -	50 -
TOTAL £ (1980-81 Cost terms) % GDP	1140 0.5	1200 0.5	1410 0.5	1380 0.6

4. INDUSTRY, ENERGY, TRADE AND EMPLOYMENT (excluding grants to nationalised industries)

4.1. Industry

Expenditure by the Department of Industry on Regional and General Industrial Support should fall in real terms by about one third between the early 1980's and 1990-91. This fall is the effect of the assumption that support for "problem companies" would only be about £200m a year as compared with the peak of about £800m for BL and Rolls Royce in 1981-82. It is assumed that regional and other industrial support will continue at roughly the level of the early 1980's while Scientific and Technological Assistance is on a rising trend and some provision is also made for future "launch aid" projects.

TABLE 4.1
EXPENDITURE BY THE DEPARTMENT OF INDUSTRY,
(excluding assistance to steel and shipbuilding)

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	1135	1085	1170	1170
% GDP	0.5	0.5	0.2	0.3

4.2. Energy

The main items of expenditure by the Department is 1990-91 are likely to be nuclear research and development, non-nuclear research and development including that on alternative sources of energy, and payments to redundant coalmine workers (which do not count towards the NCB's EFL). These programmes are unlikely to be very sensitive to differences in economic growth in the next few years. The level of research and development expenditure on nuclear and other sources of energy, for example, will depend on forecasts of requirements and returns in the much longer term. However, £30m more has been provided for payments to redundant mineworkers in Scenario 'B' to allow for

further improvements in the terms of the scheme in order to give greater encouragement to men to leave the mines. The forecast assumes a substantial decline in expenditure on development of the Fast Reactor. If the UK enters a collaborative agreement to develop this technology expenditure could be rather higher, if a decision was taken to construct a Commercial Demonstration Fast Reactor it would be significantly higher. No allowance has been made for substantial Government expenditure on a Severn Barrage or on large-scale demonstration of wind or wave power or of combined heat and power schemes.

TABLE 4.2

EXPENDITURE BY THE DEPARTMENT OF ENERGY
(excluding grants to nationalised industries)

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	300	325	250	280
% GDP	0.1	0.1	0.1	0.1

4.3. Trade

Expenditure in 1979-80 was higher than in previous years but is expected to decline as grant in aid to the Civil Aviation Authority ends with the move to full cost pricing. Thereafter, expenditure can be expected to remain roughly constant in real terms at a level similar to that in 1980-81.

TABLE 4.3.

EXPENDITURE BY THE DEPARTMENT OF TRADE

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	230	220	220	220
% GDP	0.1	0.1	0.1	0.1

4.4. ECGD

With the phasing out of loans to banks to refinance a proportion of their fixed rate sterling export lending, the main expenditure by ECGD will in future be on interest support costs. Future expenditure on this item depends heavily on market interest rates, but the total ECGD expenditure will depend on the rate of repayment of outstanding refinance.

TABLE 4.4.

EXPENDITURE BY ECGD

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	- 55	305	150	150
% GDP	-	0.1	0.1	0.1

4.5. Employment

Much of the Department of Employment's expenditure is related to the state of the labour market. But this does not imply that, in all cases, expenditure can simply be projected on that basis.

Likely policy reactions to continued high levels of unemployment are difficult to judge. But past experience indicates that expenditure on special job creation measures should most realistically be projected on the basis that it is broadly proportional to the level of unemployment (ie negatively correlated with GDP growth). Some allowance should also be made for pressures over time to contain the unit costs of schemes which take on a permanent status.

Expenditure on redundancy payments is also related to unemployment, though to its assumed rate of change rather than its level.

However, it is doubtful whether there is any straightforward correlation between expenditure on training and the growth of GDP. Following the introduction of the Youth Training Scheme, such expenditure is planned to reach £1.5 billion in cash terms in 1984-85. It may be that faster growth could provide both the incentive and the means for employers to conduct and pay for more of their own training. Alternatively, there could be pressure for more public expenditure to accelerate the process of economic adaptation. These conflicting possibilities cannot be satisfactorily reconciled, and it would be entirely speculative to assume any shift in policy to require employers to increase their contribution to training costs. The projections are therefore based on the maintenance in real terms of planned training expenditure in 1984-85.

TABLE 4.5.

EXPENDITURE BY THE DEPARTMENT OF EMPLOYMENT

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	1455	2216	2320	2660
% GDP	0.6	0.9	0.8	1.1

4.6. Total expenditure on Programme 4, excluding assistance to nationalised industries is shown in Table 4.6.

TABLE 4.6

EXPENDITURE: INDUSTRY, ENERGY, TRADE AND EMPLOYMENT
(excluding grants to nationalised industries)

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	3065	4151	4110	4480
% GDP	1.3	1.8	1.2	1.6

5. GOVERNMENT LENDING TO NATIONALISED INDUSTRIES

5.1. Grants to and borrowing by nationalised industries are incorporated in Section 16. Grants are subtracted from Programmes 3, 4 and 6 to avoid double counting. It is more appropriate in the context of the study to consider Nationalised Industries' demands for external financing as a whole than to separate grants and borrowing as is done in Cmnd 8494.

6. TRANSPORT (excluding grants to nationalised industries)

Roads and Local Transport

6.1 Transport is not mentioned in the 1979 Manifesto, and there is some flexibility about levels of expenditure. Successive Roads White Papers have however identified infrastructure projects which assist industry and improve the environment as a priority.

6.2 In general, demand for expenditure on roads reflects the need to increase road space as traffic grows and to prevent uneconomic deterioration in existing roads with later increased costs of repair. Demand for local expenditure on public transport reflects in part objective difficulties of adapting traditional services to increasing competition from the private car and in part subjective judgements of the need to provide services at less than cost to various classes of traveller or to all.

6.3 Road traffic - both private car and lorry - is forecast by Department of Transport to grow despite increasing fuel prices throughout the period and for some decades beyond. If GDP grows at the upper end of the range considered traffic is likely to increase faster than Department of Transport plans at present assume.

6.4 Even though much of the motorway construction programme begun in the 1960s has been completed pressures for expenditure on road construction are likely to continue during the period. The emphasis may begin to shift away from inter-urban road building towards faster improvement of urban roads which will otherwise become increasingly congested. The need for road maintenance is likely to increase particularly in Scenario A. Although levels of expenditure on roads will remain therefore to some extent discretionary substantial reductions might add to costs in the longer term.

6.5 Demand for expenditure on local public transport is unlikely to decrease and there is a contingent threat, unless current policy conflicts with the GLC and Metropolitan Counties are satisfactorily resolved, of increases amounting to £½ to £1 billion by the end of the period.

6.6 The projections in Table 6.1 therefore assume that cost terms expenditure will continue to absorb about 1.1 per cent of GDP in both scenarious.

TABLE 6.1 EXPENDITURE ON ROADS AND LOCAL TRANSPORT*

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 Cost terms)	2410	2390	3250	2640
% GDP	1.1	1.1	1.1	1.1

*Grants to nationalised industries are covered in a separate note

6.7 Transport (excluding Roads and local transport and grants to nationalised industries): The items of expenditure covered in the part of the Department's programme are related to its administration, research and licensing. To be broadly consistent with assumptions for the rest of the programme, they are assumed to change in line with the assumed change in GDP (Table 6.2)

TABLE 6.2 EXPENDITURE ON TRANSPORT (EXCLUDING ROADS AND LOCAL TRANSPORT AND GRANTS TO NATIONALISED INDUSTRIES)

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 Cost terms)	290	288	280	240
% GDP	0.1	0.1	0.1	0.1

Note: Includes expenditure by DOE on other transport services

6.8 Total expenditure covered in this part of the Transport programme is summarised in Table 6.3.

TABLE 6.3

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	2700	2678	3530	2880
% GDP	1.2	1.2	1.2	1.2

7. HOUSING

7.1 Public expenditure on housing has fallen sharply over the last few years. This has resulted from substantial rent increases (which have reduced subsidies from central government and from rate funds by more than 50 per cent), combined with less capital expenditure on new dwellings by local authorities, and an increase in receipts from sales under the 'Right to Buy' legislation in the 1980 Housing Act.

7.2 These trends are unlikely to continue beyond the present financial year. Further increases in the real level of rents would be largely offset by higher rent rebates (now part of Unified Housing Benefit, covered by programme 12), so that there would be little net gain to public expenditure. Some increase in gross capital expenditure is needed simply to maintain the habitability of much of the existing stock and to replace significant numbers of post-war dwellings built by industrial methods that are now becoming structurally unsound and in many cases are completely uneconomic to repair. The peak in sales will be this year; capital receipts thereafter are expected to decline.

7.3 Housing expenditure is likely to be greater in Scenario B than in Scenario A. Private sector housebuilding would probably be lower, so that more public sector expenditure would be needed if the demand from newly-formed households was to be met and the condition of the stock maintained at a level necessary to avoid a reverse in the steady post-war rise in housing standards. Sales might be lower if tenants were deterred from buying by higher mortgage rates; while the effect of these two trends on net capital expenditure, and the higher level of nominal interest rates, would increase the costs charged to Housing Revenue Accounts and thus the need for subsidy.

7.4 In constructing projections of housing expenditure in 1990-91, it has therefore been assumed that in Scenario A the same share of GDP is devoted to housing at the end of the decade as in 1982-83 while in Scenario B it has been assumed that the share will rather less than double, with the level of provision being about the same as in 1979-80.

HOUSING (England)	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	5541	2895	3500	5500
% GDP	2.3	1.2	1.2	2.2

8. OTHER ENVIRONMENT SERVICES

8.1 Expenditure covered by this programme has fallen in cost terms since the mid-70s. This mainly reflects reduced levels of capital expenditure by the Regional Water Authorities (RWAs) and of capital expenditure on local environmental services (refuse collection and disposal, recreation, administration offices and services, environmental health etc). Partially offsetting these reductions has been an expansion in expenditure on urban areas, both under the Urban Programme and by the newly-created Urban Development Corporations. The reductions themselves do not however reflect a continuing decline in requirements and are not sustainable indefinitely.

8.2 In previous years, capital expenditure by RWAs has counted in PES, but it is now proposed that only finance provided by central government (grants and loans) should be included in the main programme, with net market and overseas borrowing and leasing included in the planning total. The figures in the table below are adjusted to reflect this change in treatment; for convenience and consistency with the treatment in this exercise of nationalised industries, the total External Financing Requirement is included. There has been a corresponding change to programme 3 to exclude land drainage capital expenditure by RWAs.

8.3 About three-quarters of the expenditure in programme 8 is carried out by local authorities. Under block grant, local authority priority on current expenditure on particular services (and hence the amount falling under different programmes) is largely a matter for each authority's discretion. The same applies to capital expenditure, under the new capital control scheme. Partly because of this local discretion and partly because of uncertainty surrounding expenditure in urban areas and the financing requirement of RWAs, it is difficult to establish an objective basis for determining likely expenditure trends for this programme. Nor is it clear what effects different economic scenarios might have, since higher rates of growth while possibly reducing the net cost of urban expenditure are likely to place additional strain on water and other infrastructure. It is therefore assumed that the level of provision will be the same in both scenarios, and will in 1990-91 be 10% below the 1980-81 level.

Because of the reductions already achieved since 1980-81, and assuming the EFR of the RWAs continues to decline in cost terms, this allows for some necessary recovery in expenditure on capital programmes from the present level, assuming always that current expenditure is successfully restrained.

TABLE 8.1 EXPENDITURE ON OTHER ENVIRONMENTAL SERVICES

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	3389	3117	3000	2840
% GDP	1.4	1.3	1.0	1.2

NB Figures for 1990-91 include RWAs' total external finance, and exclude their capital expenditure

9. LAW ORDER AND PROTECTIVE SERVICES

9.1 The Government places considerable emphasis on the maintenance of law and order. Specifically, authorised police establishments and actual strengths are likely to respond to crime, and other pressures. The need to achieve alignment in prisons between resources and demand is likely to present pressing problems. Following a review of the longer term prison building programme, central departments are now considering prison service manpower, the largest element of prisons current expenditure.

9.2 Although the programme is dominated by current expenditure on the police, there is no simple determinant of expenditure. For illustrative purposes the projections are based on:-

a. the projected change in population of England and Wales (plus 2% - 1980 to 1990). It is assumed that the demand for policing grows pro rata with population, other things being equal, and this increase is reflected elsewhere in the criminal justice system;

b. an assumption that the number of serious offences recorded per head of population increases by about one third over the decade, ie broadly in line with Home Office projections, themselves based on trends. Among the other factors which might lead to their modification is the change in composition of the population. For example, although the total population is forecast to increase (see para 9.2a), the number of males in the 15-24 age group, an important client group, is expected to decline by 3% over the decade and the 10-14 age group by over 25%;

c. expenditure is assumed to increase at about half[+] the rate of "demand", reflecting improved efficiency and the effect of continuing downward pressure on public expenditure as a whole in the long run.

[+] If expenditure increased at $\frac{2}{3}$ the rate of 'demand' rather than $\frac{1}{2}$ the rate, the assumed expenditure in 1990-91 would be increased by some £200m.

TABLE 9.1 EXPENDITURE ON LAW ORDER AND PROTECTIVE SERVICES

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	3049	3417	4070	4000
% GDP	1.3	1.5	1.4	1.6

10. EDUCATION, SCIENCE, ARTS AND LIBRARIES

10.1 The projections for education have been calculated from a disaggregated analysis of the programme. Each major heading has been projected on the basis of underlying demographic determinants where these exist: for example, on the number of children of primary school age, and on a judgement of the levels of provision broadly consistent with the policies underlying the Government's present expenditure plans. These policies are aimed at 'maintaining and improving the quality of education' (Cmnd 8175) to the extent that overall expenditure constraints permit, and are thus largely determined by those constraints; the projections therefore are illustrative only. In the case of capital and some other expenditure there is no simple relationship available for converting demographic and other determinants into a demand for a stock of buildings.

10.2 The demographic basis for the projections is summarised in Table 10.1 for England and Wales.

TABLE 10.1: INDEX OF POPULATION

Age Group	mid 1980	mid 1990
3-4	100	130
5-10	100	96
11-15	100	74
16-18	100	85
19-22	100	104

Source: OPCS population projections 1979-2019

These figures disguise the reduction in the primary school age group in the early 1980s which is followed by an upturn between the mid 1980s and 1991. This upturn is not reflected in the 11-18 age group in the period up to 1991. The 19-22 age group peaks in the early/mid 1980s and declines thereafter. The demographic determinant is most important in the area of compulsory schooling (5-16). Outside this area, that is provision for under fives, for those over school leaving age in school, and for higher and further education (including

adult education and the youth service), there is some discretion over the numbers of pupils or students admitted - although present policy, which reflects the relevant statutory provisions, is to meet demand from 16-18 year olds for full-time courses in school or college.

10.3 The projections of current expenditure for the compulsory age groups are based on broadly constant levels of provision per pupil taking 1980-81 as a base, but with some allowance for diseconomies of scale as pupil numbers fall.

10.4 The main assumptions about the other areas of expenditure are the following:

a. funding of nursery education based on half the change in the numbers of 3 and 4 year olds implying a decline in participation rates from 40% in 1980-81 to a little over 30% by 1990-91;

b. funding for 16-18 year olds in schools and for all students on non-advanced courses in colleges according to projections of demand;

c. provision for higher education (including universities) is assumed to fall by about 10% up to the mid 1980s and then decline further in line with the size of the 19-22 age group. It is assumed that this will lead to a reduction in participation rates from nearly 13% in 1980-81 to just over 11% by 1990-91;

d. capital expenditure programmes set to stabilise after 1984-85 at some two-thirds of the level in 1980-81.

10.5 The residual components of the programme (mainly science, arts and libraries) are assumed to remain broadly constant throughout the period.

10.6 Constraints on reducing (in cost terms) the level of expenditure on the programme are imposed by:

a. the constitutional difficulties in securing changes in local authority expenditure (75% of the programme);

b. the contractual position of staff and the extent to which employers are willing to accept redundancies. The closure of educational buildings and staffing cuts are also constrained by national and local pressures from parents of pupils and other interest groups;

c. the high proportion (65%) of the programme which is spending on staff salaries.

10.7 In practical terms, pressures to maintain expenditure levels above those implied in the projections, for example to expand above those implied in the projections, for example to expand the curriculum and to increase participation rates outside the compulsory school age group, may be very great, especially if national income is increasing relatively rapidly.

TABLE 10.2: EXPENDITURE ON EDUCATION, SCIENCE, ARTS AND LIBRARIES

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	11027	10610	10400	10200
% GDP	4.6	4.5	3.5	4.2

11. HEALTH AND PERSONAL SOCIAL SERVICES

11.1 Expenditure on the NHS and PSS needed to provide a given standard of service is determined mainly by demographic change (that is, changes in the total size and age structure of the population), by progress in medical science (including the development of new and better surgical procedures, methods of diagnosis and pharmaceutical products), and social trends affecting eg the number of children in care.

11.2 As regards demography, total current expenditure on the Hospital and Community Health Services in England would rise by about 0.7 per cent a year during the 1980s, if current provision per head in each of the main age groups remained constant. An equivalent figure for expenditure on personal social services is 0.6 per cent in the number of men and women aged 75 and over between 1980 and 1990, compared with 2 per cent for the population as a whole.

11.3 As for the cost of medical progress, DHSS had estimated that an increase in real current expenditure of about half a per cent a year is required as a contribution to the costs of medical advance to finance inescapable innovations without enforcing offsetting reductions in standards elsewhere.

11.4 For the hospital and community health services, the Government's financial provision for 1982-83 will provide for a 1.7 per cent growth in provision if savings of £39m are realised from increased efficiency (Cmnd 8494, paragraph 2.11.12 and announcement of special pay offers on 8 March). This was the last year of the commitment in the 1979 Election manifesto. Such an increase would be sufficient to provide for demographic change and inescapable medical developments, with a margin for small improvements or in mental handicap services. It would also permit some "levelling up" in those parts of the country which have had least spent on them. For 1983-84 and 1984-85 Cmnd 8494 allows for growth in services of 0.5% a year, to be provided by increases in efficiency, subject to further consideration during the 1982 Survey having regard to the availability of resources and the scope for improved efficiency.

11.5 If current policies were broadly maintained, and with no improvements in levels of efficiency, the annual increase in provision necessary at least to meet the pressures exerted by demographic change and medical advances might be of the order of 1-1½ per cent between 1982-83 and 1990-91. There are however many areas of health care where there is a pressing need for more resources: eg to improve standards in the worst mental handicap and other long stay hospitals, to make hip operations, transplants, dialysis etc more widely available, and to introduce minimum standards for maternity care. Expenditure would need to rise at 2-3 per cent a year to make significant progress in all these areas. On the other hand the Government is committed to securing progressive increases in NHS efficiency. The scope for this is subject to review with health authorities. It seems doubtful (though not inconceivable) that a cumulative improvement of 0.5 per cent a year could continue throughout the decade. The growth of the private sector may take a little of the pressure off NHS acute services. There could also be some small increases in income through charges. For these reasons it is suggested that the minimum net real growth in provision will be 0.5 per cent a year after 1984-85, on Scenario B. With a further 0.5 per cent a year efficiency savings, this would barely maintain present standards. If GDP rises faster there will be strong pressures to use some of the extra wealth to improve standards; health service expenditure normally rises as a percentage of GDP as GDP rises, because wealthier populations chose to spend more on health care, including care for the old and handicapped who depend on state services. It is therefore suggested that the net real growth in provision might be at least 1.5 per cent a year after 1984-85 in Scenario A.

11.6 Expenditure on the Family Practitioner Services is assumed to grow by 2 per cent a year in real terms after 1982-83. This is the assumption in Cmnd 8494 for the PES period, and is at present being reviewed.

11.7 These growth rates are based on the judgement that public expenditure cannot be substantially reduced by increasing income from charges within the present system of financing. Public expenditure could be reduced by radical changes within a tax based system (eg new charges, withdrawing certain services) or by shifting part of the

population (voluntarily or compulsorily) to private insurance. Such options would have major political implications and we have not allowed for such radical changes in the calculations in this chapter.

11.8 Capital expenditure on hospital and community health services, and both capital and current expenditure on central health services, are taken to remain constant in real terms.

11.9 Expenditure on the personal social services is estimated to have risen by some 7.1 per cent in real terms between 1978-79 and 1981-82. The provision made for 1982-83 implies a reduction; but these are services where local authorities have their own discretion. As mentioned in paragraph 11.2 above an increase in just over 0.6 per cent per annum would be needed just to keep up with demographic change. There is also pressure for increased services to meet existing deficiencies and to complement Home Office provision for children (residential care orders, intermediate treatment). An increase of 1 per cent a year in current expenditure in volume terms from 1982-83 is assumed here for Scenario B and 3 per cent on Scenario A. Capital expenditure is taken to run level in real terms, income from charges is taken to rise pro rata with current expenditure.

11.10 The relative price effect for pay is calculated for the NHS and personal social services together on the same assumption as those applied to other public services. For the hospital and community health services the RPE on current expenditure other than pay has been estimated at 1.5 per cent over the period 1976-1980. Whether this RPE will continue is very uncertain, but the same figure has been used here for the period beyond 1982-83 for the purposes of calculation only. For the Family Practitioner Services the relative price effect on current expenditure other than pay is put at 2.5 per cent a year over the period 1976-80 and is again used for the purposes of calculation with the same qualifications applying.

TABLE 11.1 EXPENDITURE ON HPSS IN ENGLAND (NET OF CHARGES)

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	10494	11341	14110	13330
% GDP	4.4	4.8	4.8	5.4

12. SOCIAL SECURITY

12.1 The Scenario B projections are based on price protection of all benefit levels, no changes in eligibility for benefit and no changes in current take-up assumptions. Scenario A assumes a 1 per cent per year growth in the real value of existing benefits. This is assumed to cover also any structural improvements. This would not cover any major development such as the introduction of a comprehensive disability benefit (which might cost up to some £3b pa). In both Scenarios benefits are assumed to fall relative to wages.

12.2 A number of benefits are covered by legislation requiring annual uprating in line with prices. In some cases, such as pensions, there are firm Ministerial commitments to increase benefits in line with inflation. Supplementary benefit and child benefit is in practice increased in line with prices. Child benefit has been increased in line with inflation in 1981 and 1982. In both cases there is considerable political pressure at least to maintain the real value of the benefits.

12.3 The base taken for the projections to 1990-91 is that of the 1982 White Paper. Apart from the uprating assumptions mentioned above, the major determinants of expenditure in 1990-91 are:

i. demographic (in particular the number of pensioners and of children);

ii. unemployment (both number and composition of the unemployed);

iii. the growing maturity of the new pension scheme;

iv. increase in the population qualifying for certain benefits (eg sickness benefit and contributory benefits payable to married women).

12.4 Approximately half of the programme is accounted for by retirement, widows' and invalidity pensions. The number of pensioners will not increase greatly by 1991 (although thereafter the number of retired persons as a percentage of the working population increases rapidly). Nor does the new earnings-related pension scheme

have any major impact during the 1980s. For child benefit the number of 0-16 year olds had been used as an indicator. The population projections show this number falling until 1986 and recovering by 1991 to current levels.

TABLE 12.1 EXPENDITURE ON SOCIAL SECURITY

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	22878	26646	28560	27320
% GDP	9.6	11.3	9.7	11.1

13. OTHER PUBLIC SERVICES

13.1 Expenditure on Other Public Services is subject to periodic increases depending on the timing of Parliamentary elections and censuses. Apart from these items, and the change to Trading Fund status for HMSO, expenditure has been roughly constant in cost terms over the past few years. Most of the programme is accounted for by the costs of the Inland Revenue and Customs and Excise.

13.2 A major item of expenditure occurring after the current Survey period is the computerisation of PAYE, which will involve capital expenditure of around £200m, but result in large savings of staff costs. Apart from this change, the figures below assume that the level of expenditure on this programme remains broadly constant in cost terms.

TABLE 13.1: EXPENDITURE ON OTHER PUBLIC SERVICES

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	1143	1140	1160	1140
% GDP	0.5	0.5	0.4	0.5

14. COMMON SERVICES

14.1 Two major items of expenditure under Common Services are accommodation services, provided by PSA, and civil superannuation.

14.2 A recent PSA report suggested that, with the cuts in the civil service presently planned, rationalisation of the estate could lead to savings of £37m pa (including rates) in London alone. However, offestting this saving is the need to catch up with capital and maintenance expenditure which have been postponed to reduce the present level of expenditure. Only modest savings beyond those already identified may therefore be possible, unless civil service numbers are further reduced. The figures below assume further savings in cost terms up to the mid 1980's and thereafter a level programme.

14.3 Expenditure on civil superannuation is also partly dependent on the size of the civil service, both because of the additional costs of early retirement schemes, and through the effects on the total number of public service pensions. While showing quite a considerable increase in present plans, due to a retirement 'bulge' (including voluntary early retirement), expenditure in cost terms is expected to revert to a level about 10 per cent higher than that in 1980-81.

TABLE 14.1 EXPENDITURE ON COMMON SERVICES

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	1195	1358	1170	1100
% GDP	0.5	0.6	0.4	0.4

15. SCOTLAND, WALES AND NORTHERN IRELAND

15.1 Projections for territorial programmes have been made using present assumptions for the relationship between them and relevant English programmes. Expenditure outside the territorial blocks is assumed to remain broadly at its 1982-83 level in cost terms.

TABLE 15.1 EXPENDITURE IN SCOTLAND, WALES AND NORTHERN IRELAND

	1979-80	1982-83	1990-91	
			A	B
Scotland £m (1980-81 cost terms)	5216	5043	5570	5650
Wales £m (1980-81 cost terms)	2087	2016	2290	2250
Northern Ireland £m (1980-81 cost terms)	2888	2950	3130	3110
TOTAL £m (1980-81 cost terms)	10,191	10,009	10,990	11,010
% GDP	4.3	4.4	3.8	4.5

16. NATIONALISED INDUSTRIES

A - GENERAL

Existing Policies

16.1 The Government's policy towards the nationalised industries has three major long-term elements:

i) Financial targets. These take account of the need for investment programmes as a whole to earn a 5 per cent real rate of return, and of further moves to economic pricing. Financial targets are in place for most of the industries, the main current exceptions being loss-makers such as the National Coal Board, the British Steel Corporation and British Shipbuilders. The British Railways Board at present only has financial targets covering Sealink, the Inter-City services and the freight business. Loss-makers in most cases have a long-term duty to break even after grant.

ii) Improvements in efficiency both as a result of closer scrutiny by the Government and the Monopolies and Mergers Commission, and through greater competition. The setting and monitoring of performance aims will also have a part to play.

iii) Privatisation of both whole industries and individual activities and assets. By the early 1990's it is reasonable to assume that the whole of British Airways, and parts of the British Steel Corporation and British Shipbuilders, will have been returned to the private sector, in addition to the British Transport Docks Board and Britoil (which are expected to be privatised within the next year). British Telecom may also have been privatised, although this is still subject to substantial uncertainty. Where an industry or activity with a positive external financing requirement is being returned to the private sector, this will lead to continuing reduction in public expenditure; but most privatisation candidates are

profitable and have small or negative external financing requirements. In these circumstances, there will be no continuing net benefit to the Exchequer after the original sale has been made. The proceeds from sale will generally be counted as part of the special asset disposals programme, and so will have no net effect on total external finance for the nationalised industries.

16.2 Cmnd 8494 carried these policies forward on the basis of a forecast reduction in total external finance for the nationalised industries from £2.7bn in 1982-83 (before adjustment for the effects of the National Insurance Surcharge reduction) to £2.1bn in 1984-85. This expected improvement is also associated with a modest resumption of economic growth.

Long-Term Prospects

16.3 Forecasts of the difference between industries' total revenues and expenditure in cash terms are subject to greater uncertainty than are forecasts of other items of public expenditure; even the later year plans in Cmnd 8494 are subject to large margins of error. Forecasts for the early 1990's cannot give more than a rough indication of possible changes. However, assuming the continued implementation, and success, of the Government's policies, the following general picture emerges:

i) Investment The level of investment will depend in part on economic growth. But many of the industries have excess capacity at present; in others current investment may well be occurring to save costs rather than increase capacity; in yet others output levels and hence investment may be more or less invariant to economic growth. For example, the electricity industry currently has a large quantity of spare capacity; NCB output may be invariant to growth, and the Gas Corporation may well need to invest more with higher growth. Whether the real level of investment changes significantly may well depend above all on changes in technology - eg in the energy sector. Overall, total nationalised industry investment is unlikely to expand very much in real terms from its present level. For the purpose of this paper a reasonable assumption is that it

will remain constant.

ii) Internal resources Assuming some modest continuation of economic growth, continued restraint on current costs and improvements in efficiency, the industries' internal resources should increase steadily, although even this judgment is hazardous. For example, price competition - itself aimed at improving efficiency - would tend to reduce the industries' operating profits. Movements toward economic pricing may in any event be more or less complete by the mid-1980s.

iii) External financing In the absence of a major increase in investment, and assuming that the industries' internal resources continue to improve following the implementation of the Government's policies, the nationalised industries' external financing requirements should continue to decline gradually. Within the total, finance for the two main loss-makers (the National Coal Board and British Rail) - already responsible for threequarters of the nationalised industries total external finance in 1981-82 - will remain predominant. In turn, grant would probably account for the majority of nationalised industry external finance, as is planned for 1982-83. But the pattern depends particularly heavily on the future of British Telecom. If the industry remains in the public sector, and has a continuing large investment programme, there could well be a large external financing requirement - perhaps as high as £500m.

16.4 The projections assume continued implementation and success of government policies in all industries and the picture they show is thus arguably an optimistic one. Some account needs to be taken of important risks - for example that growth will be lower than expected, that hoped-for improvements in efficiency will not fully materialise; and that world energy prices grow more slowly than at present projected. Adverse developments even in one or two industries could well cause the outturn to be significantly worse than the total of the individual industry figures implies. To provide a more realistic view of the prospect for nationalised industries as a whole, a contingency margin of £300m - not allocated

to any individual industry - has been included in the aggregate figures for Scenario A and Scenario B.

16.5 This produces the following picture for the nationalised industries as a whole (including in both cases an assumed £500m for British Telecom).

Table 16.1

NATIONALISED INDUSTRIES' EXTERNAL FINANCE
(excluding Civil Aviation Authority)

£ million, 1980-81 cost terms

	1979-80	1982-83*	1990-91	
			A	B
Borrowing	1,796	778	700	690
Grants	1,280	1,515	870	920
Total of individual industries' external finance	3,076	2,293	1,570	1,610
Contingency margin	-	-	300	300
Total external finance	3,076	2,293	1,870	1,910
% GDP	1.3	1.0	0.6	0.8

*Figures do not take account of adjustments to EFLs in light of NIS reduction and other changes.

NOTE: Rough adjustments have been made to Programmes 4,6, 8 and 15 to take account of grants to nationalised industries scored as external finance.

National Coal Board

The plans prepared by the Board project declining external financing requirements, particularly through the late 1980's, and a return to profitability. These are also the aims of Government policy. Although capital investment might grow in real terms towards the end of the decade, the key question is how fast the Board's performance on revenue account can improve. Given the difficulties

of adjusting NCB output, higher economic growth with attendant increased energy demands ought to improve this performance and continued emphasis on cutting costs should also lead to a marked improvement over the coming years. In 1980-81 cost terms, it is assumed that the total external financing requirements of the Board will fall from some £1100m in 1981-82 including some £500m in grants to some £200m-£400m, including £100m-£200m in grants, in 1990-91 in Scenarios A and B respectively.

Electricity Supply Industry

The Electricity Supply Industry in England and Wales is projecting some real increase in capital investment during the latter half of the 1980's. Assuming that no significant change is made to the current approach to pricing, the industry should continue to make significant profits before interest. It has been assumed, therefore, that the current negative external financing requirement would become zero by 1990-1991. It has been assumed that there will be no further investment in generation in Scotland following Torness so that the combined external financing requirements of the Scottish Electricity Boards might also fall to zero by 1990-1991.

British Gas Corporation

British Gas Corporation's investment is currently at a high level, owing to the development of the Rough and Morecambe fields and the strengthening of the national transmission system. As these projects are completed and with the privatisation of the Corporation's peripheral activities, there should be a substantial reduction in the Corporation's investment in the later 1980's. On the revenue side, the gas levy can be adjusted to fine-tune the Corporation's net income. Assuming a continued policy of economic pricing, it is likely that BGC will have a zero or negative external financing requirement in 1990-91. In Scenario B, it could have a more substantial negative EFR, at the same rate of gas levy, since the need to develop new capacity and more costly sources of gas would be deferred.

BNOC

BNOC should be taken out of the calculations given the planned

privatisation of Britoil. It is assumed that the external financing requirement of the residual trading body will be negligible.

British Steel

Present policy is to return individual businesses to private hands and to close any unprofitable rump. The speed of moves in this direction will only partially depend on UK economic growth and steel demand, and the £/DM exchange rate (European steel prices are effectively denominated in DM). The assumption is that privatisation and/or closure is complete or at least that any plant remaining in the hands of the State has no EFR.

British Telecommunications

If BT has not been privatised by 1990-91, its external finance will depand on 3 main factors: its efficiency; the extent to which competition (where it can be introduced) still enables it to maintain a high self-financing ratio; and the scale of its investment programme. One possibility is that its investment requirements may tail off after the present bout of modernisation is completed in the late 1980's. But technological change and the wider exploitation of profitable opportunities in "teletronics" could well mean a continuing high investment programme. On this assumption, a figure of £500 million has been included in both scenarios.

Post Office

In recent years the PO has been a small net repayer of debt. In spite of changes which may affect its business during the 1980's - electronic mail, cable systems, etc, it is assumed that there will be no external finance requirement in either scenario.

British Airways

The Government's policy is to privatise British Airways as soon as practicable. It is assumed that profitability and/or capital reconstruction allows this to occur by the middle 1980's.

National Bus

NBC has been set financial targets which, if met, ought to ensure that there is an operating surplus which, together with depreciation, should cover investment. Such a position should obtain in both scenarios A and B. NBC also receive grants from local authorities which are expected to remain constant in real terms, at around £50m in 1980-81 prices.

British Waterways Board

In both scenarios, grant to the BWB is assumed to remain at around its present real level, at £30m (1980-81 cost terms). Borrowing is assumed to be negligible.

British Transport Docks Board

Assumed to be privatised.

Scottish Transport Group

The STG is not expected to be a net borrower in either scenario but is assumed to receive local authority grant totalling £15m in 1980-81 prices.

British Shipbuilders

The present policy is to eliminate subsidies and to privatise. Disposal of BS Ship repair interests and peripheral engineering establishments could take place before the election and privatisation of Vickers after the election, but the prospects are speculative. While direct production subsidies for merchant ships will have ended (the Home Credit Scheme continuing) both merchant shipbuilding and offshore rig building are highly cyclical industries, and BS could well need further finance to cover losses on the downslopes of the cycles or to finance further contraction in both these areas. It is unlikely that contraction in BS will have run its course as early as 1999-91 but in the good years of the cycles BS could be profitable and dividend-paying though much will depend on the intensity of the Japanese and South Korean competition.

British Airports Authority

The BAA is in normal circumstances self-financing but this will not be possible during the proposed major expansion of its South East airports. On the present timetable the major part of the expenditure on this programme is not expected to be completed until 1990 at the earliest. Depending on the growth of traffic the programme could be extended into the mid-1990s. In any case a requirement for a small EFL (of say £30m in 1990-91) could emerge.

British Rail

In both scenarios the level of grant might be expected to decline from its present historically high point which is due in part to the depth of the recession. Borrowing, on the other hand, is at a historically low level, due to the historically low levels of investment which result from the Board's decision to restrict capital expenditure to reduce their need for external finance.

The future level of both grant and borrowing will depend on BR's ability to restrain their current costs. The forecast assumes that the Board will succeed in reducing their costs in accordance with Government policies and make other changes, including investment, to adapt the railway to the needs of the modern community.

Assuming grant declines to the mid-1980s and then remains constant, and a modest programme of investment (including electrification) peaking in the mid-1980s, the Scenario A case produces borrowing figures of £30m-£50m at 1980-81 prices in 1990-91 and grant of £650m-£700m. Scenario B assumes lower investment and net borrowing of some £20m-£40m. Grant, of around £600m-£650m, would however be likely to be lower than in Scenario A because of the lower assumed growth of wages. (For the purpose of constructing aggregate figures, the mid-points of these ranges have been taken.)

Civil Aviation Authority /not strictly a nationalised industry/

Once the major programme of re-equipment is completed capital expenditure should decline and a zero borrowing requirement is projected for the early 1990's. The requirement for a Scottish Development Department grant towards the costs of Highlands and Islands aerodromes is expected to remain constant in real terms, at around £4m at current prices.

17. ASSET SALES, CONTINGENCY RESERVE AND DEBT INTEREST

17.1 Asset sales are assumed to be largely complete by 1990-91, but this depends on the timing of decisions yet to be taken. The assumed rate of sales during the 1980's affects the projected demand for external finance for nationalised industries at the end of the decade.

17.2 The Programme Totals for 1990-91 include a 2 per cent Contingency Reserve, similar to that for 1982-83.

17.3 Projections of net debt interest are very uncertain. However, it is assumed to decline to 2 per cent of GDP in Scenario B; and in Scenario A, with lower inflation and interest rates, it is assumed to decline to 1.5 per cent of GDP.

TABLE A

RATIO OF PUBLIC EXPENDITURE TO GDP[1]

	A	B
1963-64	)	34.3
1964-65	)	34.1
1965-66	)	35.3
1966-67	)	36.6
1967-68	) not	40.2
1968-69	) available	38.5
1969-70	)	37.8
1970-71	)	37.9
1971-72	)	37.8
1972-73	)	38.7
1973-74	)	40.4
1974-75	46.2	45.3
1975-76	46.2	45.7
1976-77	44.5	43.5
1977-78	40.3	39.7
1978-79	41.2	40.9
1979-80	41.0	41.2
1980-81	43.6	43.8
1981-82[2]	44.8	44.6

NOTES

(1) The two columns correspond to two definitions of public expenditure. Column A is total public expenditure as defined in the report on Long Term Public Expenditure. Figures on this definition cannot be taken back beyond 1974-75, since figures for nationalised industries' market and overseas borrowing are not available for the earlier years. The series in Column B excludes nationalised industries' market and overseas borrowing throughout.

(2) Estimated outturn, subject to revision.

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Prime Minister

(2)

I'm asked for clarification of this point (see papers attached).

MCS 21/4

Treasury Chambers, Parliament Street, SW1P 3AG

Michael Scholar Esq
No. 10 Downing Street
London SW1

21 April 1982

Dear Michael,

LONG TERM PUBLIC EXPENDITURE PROSPECTS

You telephoned last week to ask for some clarification of the remark in Sir Keith Joseph's letter of 8 April to the Chief Secretary about the draft paper for the Expenditure Steering Group on Education that the Treasury were "conducting the Chancellor's examination of long-term public expenditure prospects in terms of volume with RPE".

It is indeed correct that the working papers for this exercise are at present being prepared in cost terms, without prejudice to how the outcome of the examination should in due course be presented to Ministers.

As to the latter, there are various possibilities, and the Chancellor and the Chief Secretary will be considering them. Perhaps the most useful would be to express the possible cost of individual expenditure programmes by the end of the decade in terms of a proportion of GDP. But it would also be possible to give the figures either in cash (with specified inflation assumptions) or in cost terms, which would eliminate the effect of general inflation in the economy.

The use of cost terms as, so to speak, the working language of the study reflects its essential purpose, which is of course wholly different from that of the annual public expenditure exercise. The latter is intended to produce control totals, expressed as the amounts of cash to be spent on the various expenditure programmes. The longer term exercise is not intended to produce any sort of control totals. Its aim is rather to illustrate, on a set of economic, demographic and other hypotheses (including changes in the relative prices of particular kinds of expenditure where these seem likely to be great) what public expenditure may be building up to in the longer term, assuming the present stance of Government policy towards particular programmes.

yours sincerely

pp T F MATHEWS
Private Secretary

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21 APR 1992

PUBLIC EXPENDITURE

It is hoped that this brief will be useful to Members during the debate on the Public Expenditure White Paper (Cmnd. 8494) on 21st April.

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Conservative Research Department,
32 Smith Square, London SW1

LMR/JV
19.4.82

The Government's Public Expenditure Plans

The Government's revised expenditure plans for 1982-83 onwards are higher than the cash equivalent of those in the March 1981 White Paper. For 1982-83, as already announced, the planning total is £115 billion, some £5 billion more than the earlier plans. For 1983-84 and 1984-85 the provisional planning totals are £120 billion and £128 billion respectively, following the Budget changes.

The main increases in the plans for 1982-83 shown in the White Paper are for local authority current expenditure (£1.3 billion), nationalised industries' total net external finance (£1.3 billion), social security (£0.9 billion), employment services (£0.8 billion) and defence (£0.5 billion). These increases will be slightly affected by the Budget changes.

Total public sector capital expenditure in 1982-83 is planned to be about the same (£11½ billion) as expected in 1981-82. Expenditure on construction, following the Budget changes, is expected to rise by 14 per cent to £10¾ billion. The output from housing investment in 1982-83 should be higher than in 1981-82. There should be a slight increase int he work done on water and sewerage projects in 1982-83 compared with 1981-82. Nationalised industries' investment (including that financed from their own resources) is planned to be over £7½ billion in 1982-83, 26 per cent higher than the latest estimate for 1981-82 and 40 per cent higher than in 1980-81. In these ways the Government are planning for the continued upgrading of public services.

The Government's priorities remain unchanged. More is being spent on defence, health, employment services, and law and order and relatively less on some other programmes.

The level of public expenditure

The Government remains committed to the progressive reduction of public expenditure as a percentage of GDP. Progress has been affected by the recession - social security spending has inevitably risen while GDP has fallen. Of course, the Government has responded flexibly in the light of changing circumstances. Nevertheless:

* spending in 1982-83 is planned to be £5 billion (4½ per cent) lower than the level intended by the last Labour Government (see table on page 2);

* the level of public expenditure under this Government has not, in any year, reached that of 1974-5 and 1975-6 when it represented 46 per cent of GDP;

* recession has masked very real improvements in the underlying level of public expenditure. The benefits will become clearer as recession recedes;

* the MTFS includes a steadily declining claim by public expenditure as follows:

	1981-2	1982-3	1983-4	1984-5
Public spending as % GDP	45%	44½%	42½%	41%

..../

Planning Totals

£ billion cash

	1979-80	1980-81	1981-82	1982-83	1983-84	1984-85
Previous Government's plans (Jan. 1979 White Paper)*	80	97	110	120	-	-
March 1981 White Paper*	77.1	93.3	104.8†	110.2	113.9	-
Estimated outturns/plans in present White Paper	77.2	93.5	106.1	115.2	121.1	128.4
Changes announced in Budget and FSBR			-0.9	-0.3	-0.7	-0.7
Resulting estimated outturns/plans‡			105.2	114.9	120.4	127.6

* Converted into cash using the inflation assumption explained in part 5 of the White Paper.

† Including increases announced in the Budget on 10th March 1981.

‡ Totals do not always add up exactly, because of rounding.

The timing of public expenditure announcements

The main features of the 1982-83 plans were announced on 2nd December 1981, as soon as their broad nature became clear. Following the practice of the last two years, the White Paper (PEWP), giving a fuller account of plans for 1982-83 and the plans for later years, was published on Budget day. This allows the debate to cover both sides of the account - expenditure and taxation.

Normally, the PEWP is fairly accurate, although small changes often occur between the printing of the White Paper and the Budget statement. This year the change is relatively large - increases amounting to some £350 million are offset by savings so that the planning total in 1982-83 will be £300 million lower than in the PEWP. These changes are itemised below:

..../

Changes to the PEWP planning totals announced in the Budget statement

	£ million		
	1982-83	1983-84	1984-85
a) Added to planning total			
Provision for reduced electricity prices to large industrial users	+100	-	-
Allocation for housing improvement	+100	-	-
Contingency reserve*	+150	-	-
	+350		
b) Other changes to planning total			
Reduction in BGC's EFL (net effect after support for industrial gas prices and reduction in the gas levy)	- 73	-	-
Estimating changes in social security (mostly from 10% to 9%, reflecting improved prospects for inflation)	- 80	-225	-240
Asset sales (Wytch Farm etc.)	-100	-	-
NIS: assumed clawback from the public sector	-360	-465	-495
Net change in planning total	-265	-690	-735

* Changes in the contingency reserve include provision for restoration of the 2% shortfall on short-term benefits; for the new scheme for employment on community projects; for increased expenditure on industrial innovation; and for support for foundry coke prices.

A committee of the Institute of Fiscal Studies, chaired by the late Lord Armstrong, proposed that a draft budget, incorporating public expenditure plans, should be presented each autumn. The Treasury and Civil Service Select Committee are currently considering this proposal. The changes which have arisen this year even between printing of the final PEWP and the Budget statement underline some of the practical difficulties with this approach. While the proposals are attractive in concept, they would be extraordinarily difficult to implement.

Cash planning

The latest PEWP contains figures for expenditure which are

.../

expressed in cash rather than volume terms. This approach brings Britain into line with the other major industrial countries, and is designed to make those who manage public spending aware that, like their counterparts in the private sector, they cannot be insulated from price increases. It should encourage the trend for greater efficiency in the public sector, and ensure that the cash implications of decisions on public expenditure are fully appreciated at the outset.

Cash planning means that the expenditure plans published for 1982-83 can be translated directly into cash limits where these apply. Cash limits will not normally be revised during the year. Increased expenditure arising as a matter of deliberate policy changes will normally be charged to the contingency reserve. This will greatly facilitate control of the actual level of expenditure which occurs.

The move to cash planning has given a new impetus to the development of a much more effective range of measures of output achieved by public expenditure. Of course, in many areas such as defence, it is difficult to obtain a useful measure of output. Nevertheless, where possible these measures will increase in importance so that value-for-money is monitored rather than simply gross spending.

In setting its plans for the future, the Government did not passively accept a projected path for inflation. Rather, it has sought to influence the path of public sector costs by announcing cash plans. This will have important repercussions throughout the economy since the Government is both a major employer and a major customer for goods and services.

The degree of certainty attending cash planning totals obviously reduces in future years. To make the cash plans realistic, it is necessary that increasing provision is made in the contingency reserves in future years. The figures are:

	1982-3	1983-4	1984-5
Contingency reserve	£2.4 bn.	£4 bn.	£6 bn.

In this way, the Government is accommodating uncertainty while avoiding unconditional commitment to spending volumes irrespective of economic developments.

The Government is still considering whether, within the new régime of planning in cash, expenditure can also be expressed in 'real terms' over time. This is not straightforward. The GDP deflator can be used although it does not reflect price changes specifically in the public sector. A measure of volume (the previous practice) inevitably lumps together changes in total spending and changes in value for money achieved and is therefore of little illustrative value.

Local authorities overspent significantly in 1981-2. It is clearly impractical to attempt to claw this back in one or two years, although the Government is determined to get local authority spending back on track in future years. Planned levels for 1982-3 have been increased by £1.3 billion, and total spending will amount to £23.3 billion. Planned expenditure in 1983-4 will increase by £2.7 billion, reflecting the impact of the 1981-2 over-spend, higher housing provision and

the move to Unified Housing Benefit.

The revised figures present local authorities with a realistic target which they ought to be able to meet, albeit after making savings and economies. It is noteworthy that 70 per cent of local authority net current spending is on manpower. The reduction in numbers employed since 1979 (3%) is less than half that achieved in the civil service.

If local authorities spend in line with the Government's plans, rate increases should not be excessive, despite the reduced RSG announced in December. However, decisions in this area are for the authorities themselves, and they must take responsibility for any excessive rate increases resulting from over-spending. The Local Government (No. 2) Bill will prevent supplementary rates in England and Wales, and the whole subject of rate reform is currently under review.

Local authorities should be able to increase housing investment in 1982-3 on 1981-2, and are free to raise money for investment by selling council houses. Falling tender prices should allow services to be broadly maintained at planned levels. Provision for the Urban Programme in Great Britain is £180 million in 1982-3, half as much again as in 1981-2.

Nationalised industries' total external finance will increase relative to last year's White Paper by £1.3 billion in 1982-3; £1.7 billion in 1983-4; and £1.2 billion in 1984-5. The changed EFLs reflect government recognition of the problems caused by recession.

Total investment by nationalised industries will amount to £24 billion in the three years from 1982-3. About ⅔ of this will be financed from internal resources. Yet more could be made available by proper control of costs - each 1% on labour costs means £140 million less for investment.

The PEWP figure for receipts from special asset sales is £600 million a year from 1982-3, which is £400 million above the figure in last year's White Paper. This largely reflects the planned disposal of Britoil and some of BGC's assets. Privatisation is the best method of raising private sector capital. The gross figure for asset sales in 1981-2 is approximately £500 million, which includes proceeds from the privatisation of Cable and Wireless and Amersham International, sale of shares in British Sugar Corporation and the management buyout of the National Freight Corporation.

Public sector staffing, pay and efficiency

The Government intend to make a continuing saving in public service manpower. The civil service has been reduced from 732,300 in April 1979 by nearly 8 per cent to 675,400 in January 1982, the smallest for nearly 15 years. A further reduction is planned to 630,000 by the end of 1983-84, a total reduction of 14 per cent. The civil service will then be smaller than at any time since the end of the second world war.

An increase in services to patients in the National Health Service (NHS) implies some increase in manpower. Between 1979 and 1981, total manpower in the NHS is estimated to have increased by some 40,000 (full-time equivalents), that is, about 5 per cent. A breakdown by manpower category is not yet available for 1981, but

.../

nearly 80 per cent of the increase between 1979 and 1980 was for manpower directly involved in care of patients. In England the Government have set a target of a 10 per cent reduction over the next three years in NHS management costs as a proportion of NHS resources. Comparable measures are in hand in Scotland and Wales.

Local authorities' manpower in Great Britain has been reduced by over 70,000 (full-time equivalents), or 3 per cent, between March 1979 and September 1981. The net saving so far in local authorities' manpower is, proportionately, less than half the reduction in the civil service. Further savings are envisaged in the expenditure plans. The largest reduction has been in the education service (school roles are falling); manpower fell by nearly 60,000 or 5 per cent between 1979 and 1981, but this service still employs nearly half of local government workers. The staff employed on law, order and protective services increased by 11,000 (4 per cent) over this period, and further slight increases are planned.

Pay accounts for some 30 per cent of total public expenditure; in many programmes the proportion is much higher. Labour costs are also an important component in the cost structure of the nationalised industries. Within a framework of cash planning excessive expenditure on pay reduces the money available to finance investment or services to the public. That is why the Government is determined to maintain firm control of the public sector pay bill. It is noteworthy that, according to the New Earnings Survey, earnings in the public sector were 7% higher than in comparable private sector occupations in 1981.

Administrative costs account for almost 10% of total public expenditure. The Management and Personal Office is conducting with departments a programme of scrutinies and of reviews of the cost-effectiveness of common activities, such as stores, transport, typing and messengerial services. Together such activities constitute up to 15 per cent of the total running costs of departments. The studies in the programme so far have pointed to cost reductions averaging between 10% and 40% depending on the activity concerned. Guidelines on good practice are being disseminated to all departments and responses followed up.

Sir Derek Rayner continues to assist Ministers to improve efficiency. As a result of work already done by Sir Derek Rayner, Government has taken firm decisions which will secure £110 million a year in recurrent savings and £28 million in one-off savings.

The arguments against 'reflation'

The Government's critics argue that rising unemployment demands increased public spending and borrowing which would allegedly create jobs. Few other governments are attempting this remedy. Yet unemployment is at record levels, not only in the UK, but in France, Canada and Italy. Figures in the USA and Germany are at their highest since 1935.

Most major countries - US, Japan, Germany, Italy, Netherlands, Belgium, Australia, Sweden - have recently announced measures to cut planned public expenditure. France has recently deferred £1.5 billion capital investment, despite the election of a socialist government committed to an economic expansion in public spending. The widespread realisation is that lower borrowing and lower inflation lead to

lower interest rates. This is the best way of expanding the economy and creating real jobs.

In Britain, during the 1970s, we saw at first hand the declining effect of increased public borrowing even in short-term job creation. The major effect of 'reflation' was to boost inflation and imports and undermine the economy. This led in the longer term to more, not less, unemployment. Labour recognised that in office, but the lessons learned so painfully are apparently now forgotten.

Labour's record on public expenditure 1974-9 is well documented in Joel Barnett's book "Inside the Treasury". The following series of quotations illustrates how the initial bout of profligacy was followed by a series of crises and cuts in public expenditure dictated by the IMF. "The first months of the new government (after February 1974) were characterised by our spending money which, in the event, we did not have".

"By July 1974 there was another economic statement made in the expectation of an autumn election ... there can be little doubt that we planned for too high a level of public expenditure, in the expectation of growth that never materialised".

"By March 1975, we were seeking approval for cuts of over £1 billion ... shortly after, we had what later became an almost regular July crisis".

In July 1975, the then Prime Minister, Harold Wilson "rejected 'panic cuts in expenditure'. But by the autumn, we were making 'non-panic' cuts very much larger than those announced in the Budget".

November 1975 - Labour were applying for credit to the IMF. "To get the IMF's approval, we needed extra spending cuts. For the moment, we did not find it possible to make cuts in the year immediately ahead. But we made cuts of some £1.6 billion in 1977-78, leading to cuts of £3 billion planned for 1978-9".

"At Cabinet on July 6th (1976), the Chancellor opened with his explanation of the need for a further £1 billion cut in public expenditure ... If this expenditure package was difficult, little did we know of what the autumn, the IMF and another sterling crisis had in store for us".

In 1976, another substantial request for credit from the IMF became necessary. ".... we came to the vital Cabinet (2nd December 1976) .... The Chancellor made it clear that he wanted public expenditure cuts of £1 billion in 1977-78 and substantially higher cuts in the following year".

"On December 14th, there was a long and unhappy discussion.... Peter Shore angrily said 'There is no will in this Cabinet to tell the IMF to take a running jump, even if unemployment rose to 2 million'".

This traumatic period is summarised by statistics for public expenditure (as defined in the January 1979 PEWP) as a percentage of GDP at market prices - it rose dramatically from 39% in 1973 to a record 46.2% in 1975, only to fall equally dramatically to 40.2% by 1977 (Appendix 1, "Getting and Spending" by Sir Leo Pliatzky).

Politics and Public Expenditure

The 'socialist alternative', based on massive public expenditure, was available to the last Labour Government, but they rejected it. Joel Barnett, as Chief Secretary to the Treasury, said in a speech in London on 16th July 1976, "To suggest that there is an alternative economic strategy that would allow immediate increases in public expenditure is to do a great disservice to the Labour movement, for it deludes our own supporters and does maximum harm by building up great expectations which cannot be delivered".

James Callaghan fully understood the declining potence of increased public spending as a job creator. In a speech in Woolwich on 30th January 1976, he said, "In the 1960s, when I was Chancellor, we did achieve full employment by means of a general release of purchasing power. It was successful for the time being, although it contained the seeds of long-term weakness". By September of that year, he told his own conference "in all candour" that the option of spending our way out of recession no longer existed.

Roy Jenkins, for the SDP, has suffered a similar volte face. After the 1967 devaluation, he became Chancellor and embarked upon what Sir Leo Pliatzky, in his recent book, has described as "The War of Jenkins' Cuts", and achieved the only post-war negative PSBR. Much later, in a speech in Anglesey on 23rd January 1976, when he was Labour's Home Secretary, he warned, "I do not think that you can push public expenditure significantly above 60% (of GDP) and maintain the values of plural society with adequate freedom of choice". Definitions have changed since and the level he feared corresponds more or less to the level we now have. Apparently, Mr. Jenkins now cares less about maintaining the values of a plural society, since he wants to see public spending and borrowing increase.

..../

THE FALKLAND OPERATION: THE DEFENCE COSTS IN PERSPECTIVE

The following is an extract from a speech by Mr. Leon Brittan, given in Oxford on 15th April 1982.

There is no point at this stage in trying to assess the cost of our Falklands operation. But it is right to make two points crystal clear. First, there is no cash ceiling on the cost of the operation. The needs of the Task Force must and will come first. But secondly, its cost can and will be met in ways consistent with the Government's economic strategy.

Not all of this cost will be additional. Additional expenditure arises only where the cost of the operation proves to be greater than that of the tasks to which the Forces concerned would otherwise have been assigned. At this stage the extra cost represents a very small proportion of the Defence Budget of over £14 billion. There is therefore no cash or budgetary problem immediately in prospect.

But it has been suggested that our ability to respond to the crisis in the Falklands, or others like it, has been weakened by the Government's so-called "cuts" in Defence spending. This is complete nonsense.

So far from cutting defence spending, we have actually increased it from the level of £7½ billion which we inherited in 1978-79 to over £14 billion today. This cash increase of over 85% represents a real increase of about 11 per cent.

This financial year we will be spending £½ billion more in real terms on conventional naval forces than was spent in the year before we came into office. As to the future, we will still be spending more on the conventional Navy, even when expenditure on modernising the strategic deterrent is at its peak, than in 1978-79. The Navy still enjoys as high a proportion of the Defence Budget, 28 per cent, as it did in that year, and a higher proportion than it did ten, twenty or thirty years ago.

A massive modernisation programme for the fleet is in hand. Spending on equipment will be over £3200 million in 1982-83. Our fleet submarine numbers are planned to increase by almost 50%.

Some critics have complained of the forthcoming loss to the fleet of the aircraft carriers Invincible and Hermes. This criticism is simply ludicrous, because it ignores the crucial fact that two carriers will continue to be kept in service; Illustrious, which is to replace Invincible, will join the fleet later this year, and the construction of Ark Royal, to replace Hermes, is proceeding satisfactorily. But this is not to be achieved by neglecting other aspects of the navy. In February we ordered the eighth Broadsword class frigate, and the build up of the Sheffield class destroyer force is progressing well.

These vessels will all be equipped with effective modern weaponry. The Sting Ray torpedo will enter service shortly, and the development of a new heavyweight torpedo was recently announced; The torpedo procurement programme now totals more than £2 billion. We are also bringing into service the air-launched anti-ship missile Sea Skua and the submarine launched Sub-Harpoon; the air defence missile Sea Wolf is being upgraded; and the Sea Eagle anti-ship missile is in full development.

Of course some of today's vessels will be disposed of or scrapped before long. But it is inconceivable that the pattern of our forces should remain static. The significant feature of our defence policy today is that the current programmes of modernisation and rebuilding will actually leave us with more major ships and submarines operational in 1985 than there are today. To ignore that central fact is to blind oneself to the beneficial results of the major programme of procurement upon which we have embarked, as a result of the deliberate decision of this Government to give defence spending the priority which it had previously been denied.

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19.4.82

PUBLIC EXPENDITURE

This table should have been appended to the Research Department brief PFC(82)5 circulated for the debate on the Public Expenditure White Paper on 21.4.82. We apologise for this omission.

TOTAL PUBLIC EXPENDITURE BY PROGRAMME

(excluding Budget changes)

£ million cash

	1979-80 outturn	1980-81 outturn	1981-82 estimated outturn	1982-83 plans	1983-84 plans	1984-85 plans
Defence	9,226	11,178	12,634	14,103	15,300	16,440
Overseas aid	802	919	989	973	1,040	1,110
Net payment to EC institutions	851	288	45	500	580	600
Other overseas services	454	508	613	666	700	740
Agriculture, fisheries, food and forestry	1,038	1,384	1,557	1,534	1,490	1,500
Industry, energy, trade and employment	2,892	4,190	5,602	5,845	4,860	5,030
Transport	2,972	3,487	3,922	4,160	4,340	4,490
Housing	4,699	4,675	3,320	3,480	2,760	2,860
Other environmental services	2,873	3,377	3,471	3,747	3,870	4,030
Law, order and protective services	2,586	3,180	3,747	4,108	4,450	4,700
Education and science, arts and libraries	9,350	11,376	12,362	12,754	13,110	13,410
Health and personal social services	8,899	11,366	12,764	13,633	14,480	15,250
Social security	19,400	23,440	28,618	32,030	33,500	35,400
Other public services	969	1,213	1,333	1,370	1,520	1,610
Common services	1,013	1,103	1,599	1,633	1,800	1,930
Scotland	4,423	5,292	5,722	6,062	6,270	6,490
Wales	1,769	2,124	2,288	2,423	2,500	2,610
Northern Ireland	2,449	2,902	3,276	3,546	3,780	3,990
Government lending to nationalised industries	1,857	2,276	1,816	1,114	1,260	1,140
Adjustments						
Nationalised industries net overseas and market borrowing*	−321	−448	202	−180	50	−370
Special sales of assets	−999	−356	−50	−600	−600	−600
Contingency reserve			300	2,250	4,000	6,000
PLANNING TOTAL	77,201	93,475	106,130	115,150	121,070	128,370

*Including other public corporations accorded similar treatment.

cc SU

Treasury Chambers, Parliament Street, SW1P 3AG

Rt Hon Sir Keith Joseph MP
Secretary of State
Department of Education and Science
Elizabeth House
York Road
London SE1 7PH

16 April 1982

Dear Keith,

DRAFT PAPER FOR EXPENDITURE STEERING GROUP - EDUCATION

Thank you for your letter of 8 April. with MCS ?

I am grateful for your assurances about the primacy of planning in cash and the need to ensure that local authorities do not assume that we are committed to some underlying level of provision. I am glad that your officials will make these points clear in the course of the Steering Group's discussions. As you know the Prime Minister attached particular importance to this issue. Incidentally, I do not myself see the connection you suggest between this issue and the quite separate question of the exercise on long-term expenditure prospects.

Since you wrote our officials have considered further revisions to the draft paper. These go some considerable way to meet my anxieties. I am therefore prepared to agree that a paper should be circulated in the terms now agreed.

I am copying this letter to the Prime Minister and to Sir Robert Armstrong.

Yours,

Leon

LEON BRITTAN

(2)

Prime Minister

MCS 8/4

DEPARTMENT OF EDUCATION AND SCIENCE

ELIZABETH HOUSE, YORK ROAD, LONDON SE1 7PH

TELEPHONE 01-928 9222

FROM THE SECRETARY OF STATE

The Rt Hon Leon Brittan QC MP
Chief Secretary
Treasury
Parliament Street
London
SW1P 3AG

MT

R/8 April 1982

Dear Leon.

DRAFT PAPER FOR EXPENDITURE STEERING GROUP - EDUCATION

Correspondence on this issue rests on Michael Scholar's letter to my Private Secretary of 16 March, following my letters to you of 10 and 12 March.

I would not have written to you as I did on 10 March if I had seen any possibility of my proposals putting in question the primacy of cash planning. My concern is to do all I can to ensure that local authority expenditure on education is kept down to the cash figures in Cmnd 8494. I am clear that this cannot be done effectively without illustrating to the local authorities the degree of contraction (depending upon how pay and prices move) that the Government expect them to make in their education services, in terms that they cannot fail to understand. In doing this, and in discussion in the Steering Group, both my officials and Treasury officials will of course make clear that the cash figures are the policy, and that if pay and prices go higher, then the volume of activity will have to be curtailed.

I believe that planning in cash is wholly compatible with trying to make the plans effective by translating them into action on the ground. This is indeed the message of the remit for the various Expenditure Groups which has been agreed and circulated to the local authority associations. The remit asks the Groups to frame their reports in cash but also refers to "levels of service implicit in Cmnd 8494". I am encouraged to believe that you share this view when I see that the Treasury themselves are conducting the Chancellor's examination of long-term public expenditure prospects in terms of volume with RPE, just as they deal in manpower ceilings as well as in cash to impress upon Departments the Government's policy on the civil service.

Is this correct?

On this basis I hoped that officials here and in the Treasury would be able to settle a paper for ESGE, whose meeting originally arranged for 18 March was postponed until a satisfactory paper could be prepared. In the event, despite a number of significant changes we have made in your direction, compared with the version which I sent to you on 10 March, this has not proved possible.

I really cannot see why the Treasury regard our approach, of illustrating the steps required to make a reality of the Government's cash plans, with full regard to the primacy of the cash figures, as "incompatible with the spirit of the remit" as their most recent letter says. I attach great importance to this - perhaps more than other Ministers concerned with local authority programmes - because it affects so large a proportion of my whole programme and I am much dependent on securing understanding of the Government's intentions if I am to bring local authority expenditure on education closer to our plans. I fear that a paper which gives no illustration of the required measures in illustrative volume terms will provide no basis for a constructive discussion.

For these reasons, I very much hope that you will agree that the approach in the paper in the form in which it now stands is compatible with the spirit of the remit and that it should be circulated for the meeting of ESGE on 23 April.

I am sending copies of this letter to the Prime Minister and Sir Robert Armstrong.

Yours

Keith

8 APR

a CSO

Econ Pol

10 DOWNING STREET

From the Private Secretary

1 April 1982

In the course of her briefing meeting with the Chancellor and others yesterday evening, the Prime Minister said that she hoped it was clearly understood that there should be no economies in expenditure on law and order and especially on the police, in the course of the 1982 public expenditure survey. It was on this assumption that she agreed to the inclusion of the Home Office in the exercise, without the explicit safeguards which had been extended to the Ministry of Defence.

I am sending a copy of this letter to Terry Mathews (Chief Secretary's Office).

M. C. SCHOLAR

John Kerr, Esq.,
H.M. Treasury,

CONFIDENTIAL

Econ Pol

10 DOWNING STREET

Prime Minister

Public Expenditure.

If the plan to keep the discussion low-key fails here are two points you could deploy:

(i) Public Expenditure as a % of GDP has been rising steadily since 1979. It is now around 45% – a level last reached in 1976 (figures attached)

(ii) Even after the Budget, the

real value of single and

married allowances is about 3 %

below the 1978-79 level. ~~about~~

the

MCS 31/3

Ref. A07977

PRIME MINISTER

Cabinet: Public Expenditure Survey 1982

BACKGROUND

The Chief Secretary, Treasury, circulated to Cabinet, under cover of his minute to you of 25th March, his proposed guidelines for the 1982 Public Expenditure Survey. The Foreign and Commonwealth Secretary, the Secretaries of State for Education and Science, for Northern Ireland and for the Environment, and the Minister of Agriculture, Fisheries and Food have each raised points, in correspondence dated 30th March, which need to be discussed by Cabinet tomorrow.

2. The main issue arising from the correspondence is whether Departments should identify costed options for reductions over and above any savings necessary to offset additional bids. The other points seem relatively straightforward and can either be clarified in the course of the Survey discussions or are for decision later when Cabinet comes to substantive discussions of the 1982 Survey. In view of the heavy load of business tomorrow morning, and of the fact that Ministers appear to accept most of the Chief Secretary's proposals, you will wish to focus on the points at issue and to avoid either going over the proposals as a whole or letting the discussion widen into a more general debate on public expenditure and economic policy.

3. An important general point, which the Chief Secretary will no doubt emphasise, is that the present proposals are primarily procedural and are not intended to prejudge the substantive decisions which the Cabinet will need to take in the summer and the autumn.

MAIN ISSUES

Options

4. The Chief Secretary proposes - paragraphs 12 and 13 of the Annex to his minute - that any additional bids should be accompanied by proposals for off-setting savings and that in addition to such savings Departments should identify

for every programme costed options of at least 2 per cent for 1983-84 rising to at least 4 per cent by 1985-86. For Social Security the reductions would be applied from the November uprating dates. As you know from the Chief Secretary's letter of 25th March to the Secretary of State for Defence, he has agreed that option cuts should not apply to the defence budget: it is not intended that other members of the Cabinet should know of this.

5. The Secretary of State for Education and Science, in his letter to the Chief Secretary of 30th March, argues against identifying at this stage option cuts beyond any offsetting savings. He believes - and the Foreign and Commonwealth Secretary and the Minister of Agriculture support him - that this is unnecessary in view of the options identified in previous exercises, and also potentially politically damaging if the options identified were leaked and misinterpreted. The Secretary of State for the Environment, in his minute of 30th March, proposes that, as agreed by the Cabinet last year, Departments should deal with the identification of option cuts for the local authorities and that there should be no consultation through the Consultative Council on Local Government Finance. His point is that in practice it will be difficult enough securing the local authorities' co-operation in conforming with their present programmes, let alone pressing them for reductions.

6. I understand that the Chief Secretary will probably:-

(i) Concede that as last year the local authorities should not be consulted on costed options.

(ii) Argue that it is necessary for all Departments to identify options systematically, so that later in the year the Cabinet has a basis for considering how to offset additional bids (it is probably unrealistic to assume that suitable offsetting savings will be identified to deal with all such bids) and for considering the question of whether any further savings might be made at the margin in public expenditure totals. He will probably argue that, without such a requirement on all Departments, some might volunteer savings but others might hold back. In paragraph 7.4 of his minute to you he proposes that in the first instance the costed options should not be circulated generally; in this way it may be possible to reduce the risk of leaks of sensitive options.

(iii) Argues against any suggestion, which he understands the Secretary of State for Energy might make, for excluding grants to nationalised industries from the options exercise: this would be inconsistent with the aim of looking systematically across the whole board.

Local Authority Current Expenditure

7. One of the most difficult aspects of the 1981 Survey was reaching decisions on local authority current expenditure in time for a Rate Support Grant settlement before Christmas and, in doing so, keeping in step with related decisions on central government expenditure and with the Survey exercise as a whole. The Chief Secretary has now reached agreement with the Ministers responsible for local authority programmes on certain improvements in the procedure for this year. These are summarised in paragraph 8 of the Annex to his paper.

8. The Secretary of State for Education and Science is generally satisfied with this, but, in his letter of 30th March, he emphasises the importance of conducting discussions so that he can take a sensible decision on his education programme overall, relating the local authority element to the central government expenditure. This is primarily a question for the Secretary of State to sort out further with the Chief Secretary, but it is obviously right to plan to take these decisions in an orderly manner; a similar point arises on the discussions of housing expenditure and council rents which, as you will recall, impinge crucially on the local authority decisions.

Comparability

9. In his letter of 30th March to the Chief Secretary, the Secretary of State for Northern Ireland says that he is willing to provide illustrative options for reductions provided the Chief Secretary can assure him that the "comparability formula" will again apply in determining the totals for the territorial programmes - that is, adjustments in some major programmes in Northern Ireland are made to ensure parity with the comparable programmes in Great Britain. I understand that this is acceptable to the Chief Secretary, and so it should not need discussion.

Manpower

10. The Chief Secretary proposes, in paragraph 15 of the Annex to his minute, the presentation of manpower figures in accordance with the agreed Departmental targets. In his covering minute - paragraph 7.6 - he describes this as providing "a neutral baseline for subsequent policy decisions".

11. The Foreign and Commonwealth Secretary, in his minute of 30th March, warns that further reductions beyond the agreed targets would be unacceptable to him. The questions whether there should be such further reductions, and if so where, is not for discussion at this stage.

Government Accommodation

12. Paragraph 16 of the Annex to the Chief Secretary's minute deals with the new arrangements for repayment by Departments of expenditure on their behalf by the Property Services Agency. The Foreign and Commonwealth Secretary wishes the individual requirements of Departments to be taken fully into account when this total is distributed between Departments. This is something which officials can readily deal with in the Survey discussions.

HANDLING

13. After the Chief Secretary has introduced his minute, and commented on the points made to him in correspondence, you may wish to make clear that you want to confine the discussion to the outstanding points of difficulty and not to go over the proposals as a whole.

14. On options - paragraphs 4-6 above - there is a political judgment for the Cabinet to make. In principle the Chief Secretary has a strong case in calling for the systematic identification of options from each Department. The question is whether this case is overridden by the doubts raised by some Ministers on the political difficulties which could arise from any leaks which were misinterpreted. You will want to ask those Ministers who have expressed doubts to speak to their letters: they are the Secretary of State for Education and Science and the Lord Privy Seal (in the Foreign and Commonwealth Secretary's absence). (The Minister of Agriculture who has also registered his doubts is in Brussels.) You might then invite the Chief Secretary to state his case in reply, before opening the discussion to other Ministers.

15. It should be possible for you to deal quickly with the remaining issues, listed in paragraphs 7-12 above, on the grounds that they can either be pursued further in the course of the Survey discussions or that they do not arise until the Cabinet's substantive discussions in the summer and in the autumn.

CONCLUSIONS

16. In the light of the discussion you will wish to record the Cabinet's approval of the proposals for the conduct of the 1982 Public Expenditure Survey set out in the Annex to the Chief Secretary's minute of 25th March, subject to:-

(i) A decision on whether Departments should identify at this stage options for reductions in addition to savings to offset additional bids.

(ii) Agreement that the local authorities should not be consulted on costed options through the Consultative Council on Local Government Finance.

(iii) Noting that other points raised in correspondence and in the discussion will be dealt with in the course of the Survey discussions or substantively in the Cabinet's discussion later in the year of the 1982 Survey.

RTA

ROBERT ARMSTRONG

31st March, 1982

CONFIDENTIAL

SCOTTISH OFFICE
WHITEHALL, LONDON SW1A 2AU

The Rt Hon Leon Brittan QC MP
Chief Secretary to the Treasury
HM Treasury
Parliament Street
London
SW1P 3AG

31 March 1982

Dear Leon,

PUBLIC EXPENDITURE SURVEY 1982

Thank you for sending me a copy of your recent minute to the Prime Minister. I am in general content with the arrangements you propose for the 1982 Survey. There are, however, some points arising out of your paper which I think it would be right for me to record at this stage. We may need to revert to some of them at a later stage.

We have already corresponded about the new proposals for handling local authority current expenditure. In my letter of 10 March I indicated that I should be happy to endorse the proposals on the understanding that they did not imply giving less weight than in the past to the rating effects of expenditure decisions.

On the treatment of accommodation expenditure, it is of course right that the new arrangements to operate from 1983-84 should be reflected in the baseline for the 1982 exercise but I understand that officials have not yet agreed on the basis for allocating accommodation expenditure among departments. It will be important to reach an agreed and equitable allocation if the new arrangements are to get off on the right foot and achieve the purposes for which they were devised. I presume that if officials cannot agree on such an allocation you and Michael Heseltine will bring the matter before departmental Ministers.

You refer in paragraph 7.5 of your minute to consultations with local authority representatives. I propose to follow the traditional arrangements in Scotland which entail consultation with the Convention of Scottish Local Authorities over total provision for individual services in the following financial year but not on option reductions which are dealt with internally by my Departments.

Like Jim Prior I set great store by the block/formula arrangement. But I ought perhaps to put on record my concern at the increasing problems which I shall face in dealing with local authority current expenditure. I may wish to write to you again about this when I have had a further opportunity to consider the picture which is now emerging and the prospects for rate levels in 1983.

I am sending copies of this letter to Cabinet colleagues and to Sir Robert Armstrong.

Yours ever,

George.

31 MAR 1982

DEPARTMENT OF HEALTH & SOCIAL SECURITY
Alexander Fleming House, Elephant & Castle, London SE1 6BY
Telephone 01-407 5522
From the Secretary of State for Social Services

The Rt Hon Leon Brittan QC MP
Chief Secretary to the Treasury
Treasury Chambers
Great George Street
LONDON
SW1

March 31 1982

Dear Leon.

PUBLIC EXPENDITURE SURVEY 1982

You sent me a copy of your minute to the Prime Minister about the public expenditure survey 1982.

I accept generally the proposals you have for the handling of the public expenditure survey in 1982. But I must reserve my position on the proposal that estimating increases on demand-determined services should count as additional bids. I appreciate that in some respects this has been done on previous public expenditure rounds. But it has not in practice been applied to social security expenditure. If it were, would it imply, to take a very basic example, that if our estimate of the number of people entitled to retirement pension went up, we could be required to pay for the increased estimate by reducing the real value of the retirement pension? That does not seem to me a line we could sustain. Nor would it be any easier to sustain if we were to reduce the value of any other benefit for this purpose. My position therefore must be that social security should be treated as an exception to this general proposition.

I am copying this to the Prime Minister, the other members of the Cabinet and Sir Robert Armstrong.

Yours ever
Norman

NORMAN FOWLER

CONFIDENTIAL

MINISTRY OF AGRICULTURE, FISHERIES AND FOOD
WHITEHALL PLACE, LONDON S.W.1

From the Minister

The Rt Hon Leon Brittan QC MP
Chief Secretary to the Treasury
Treasury Chambers
Parliament Street
London
SW1P 3HE

30 March 1982

30 MAR 1982

Dear Chief Secretary

PUBLIC EXPENDITURE SURVEY 1982

May I refer to your minute to the Prime Minister setting out proposed guidelines for the 1982 Public Expenditure Survey. My only comment concerns your proposal that Departments should be required to identify arbitrary percentage reductions of their baselines.

Every Department, as part of its normal resource planning, should scrutinise its programmes to identify both where new requirements may arise and where there may be scope for savings. This is a necessary part of effective forward planning which we are already carrying out within my Department in preparation for this year's Survey exercise. It is the approach recommended by the consultants who recently reviewed my Department's financial management systems.

To require that all Departments, over and above an assessment of their additional requirements and the scope for savings, report how quite arbitrary percentage reductions on their baselines could be achieved and what would be the consequences will, in my view, contribute neither to the internal reviews of Departments nor to the subsequent Ministerial discussion. It could only cast

/doubt on the ...

doubt on the outcome of last year's public expenditure review when every conceivable expenditure cut over the survey period was rigorously examined; and if it became publicly known it would give a false and demoralising impression of the Government's intentions and of our assessment of the economic situation. I hope you could agree therefore that this requirement should be dropped from the ground rules.

I am copying this to Cabinet colleagues and to Sir Robert Armstrong.

Yours sincerely

Robert Lowe

3 0 MAR 1982

PETER WALKER

(Approved by the Minister and signed in his absence)

CONFIDENTIAL

cc AW
JV

MT.

Prime Minister

PUBLIC EXPENDITURE SURVEY 1982

In paragraph 7.5 of his recent minute to you, Leon Brittan proposed that representatives of the local authorities should be consulted about the costed options relevant to them using the machinery of the Consultative Council on Local Government Finance.

I am unwilling to agree to this.

Colleagues will recall that last year the Cabinet endorsed my view that options for reductions on local authority expenditure should be examined within government but should not be remitted to the Expenditure Groups. (CC(81)22nd, Minute 5). They agree that to consult on options which the local authorities would regard as unrealistic would provoke odium disproportionate to any likely benefits; and that Departments were already in a position to assess the action which would be needed to secure cuts on particular programmes.

These arguments are equally valid this year. The cash provision for local government services in 1983-4 is already being criticised as inadequate, and it was only with difficulty that I persuaded the local authority associations, at last week's meeting of the Consultative Council, to endorse a remit for the Expenditure Groups based on the White Paper figures. If we were now to go back to local government with a proposal for a supplementary remit based on yet lower figures we should in my view risk bringing the consultative process into disrepute.

I agree that Departments should look at options for reductions. But we should follow last year's practice and keep this work within the Government machinery.

I am sending copies of this minute to Cabinet colleagues and to Sir Robert Armstrong.

D. Jenkin

p.p. MH

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

2 Mr S cc AW JV

NORTHERN IRELAND OFFICE
GREAT GEORGE STREET,
LONDON SW1P 3AJ

SECRETARY OF STATE
FOR
NORTHERN IRELAND

Prime Minister (2)
4 responses (see 3 attached)
As you suspected, a discussion looks inevitable
MCS 30/3

Rt Hon Leon Brittan QC MP
Chief Secretary
HM Treasury
Parliament Street
LONDON
SW1P 3AG

MT

30 March 1982

Dear Chief Secretary

PUBLIC EXPENDITURE SURVEY 1982 - GUIDELINES

I am responding to your proposals for the Guidelines for the 1982 Survey which accompanied your recent minute (24.3.) to the Prime Minister.

In general, I am content with what you propose. However, I note that the proposals as they now stand make no specific reference to the territorial Departments. Last year, it was agreed that the comparability formula should apply in determining the totals for the territorial programmes. As you know, we in Northern Ireland place great importance on the operation of the block and comparability arrangement and on the discretion which it provides to allocate expenditure to individual services in line with Northern Ireland needs. I should therefore be glad to have your confirmation that it is intended that the comparability arrangement should again apply to Northern Ireland for the 1982 Survey.

You will also be familiar with the point that adjustments in a number of major programmes in Northern Ireland must, because of parity considerations, follow decisions in Great Britain, and that any options for reductions which you might wish me to put forward in advance of decisions in Great Britain must therefore be highly speculative. However, if you can confirm that comparability will apply, I will be content, if you wish, to provide illustrative options for reductions on the same basis as was agreed for last year.

I am copying this letter to Cabinet colleagues and to Sir Robert Armstrong.

Yours sincerely,

M W Stephens

pp JAMES PRIOR
(Signed on behalf of the Secretary of State in his absence)

ssd

30 MAR 1982

e

CONFIDENTIAL

cc SU
AW

DEPARTMENT OF EDUCATION AND SCIENCE

ELIZABETH HOUSE, YORK ROAD, LONDON SE1 7PH

TELEPHONE 01-928 9222

FROM THE SECRETARY OF STATE

The Rt Hon Leon Brittan QC MP
Chief Secretary
Treasury
Parliament Street
London SW1P 3AG

30 March 1982

Dear Leon,

PUBLIC EXPENDITURE SURVEY 1982

Thank you for sending me a copy of your minute to the Prime Minister.

2. I have two reservations on the proposals in the Annex:-

Local Authority Current Expenditure

I have already commented in my letter to you of 10 March (copied only to colleagues with local authority responsibilities) on the proposals summarized in paragraph 8. I do not dissent from (i) and (iii); but (ii), as it is now drafted, is much too restrictive. As I said in my previous letter, I cannot accept a repetition of last year's experience when I had to take last-minute action to escape the outcome of separately deciding the local authority and the Vote components of my education programme in two different Cabinet committees, with no opportunity for me to strike an acceptable balance between the two. We must ensure that our decisions on local authority expenditure at each stage are taken not in isolation but in the appropriate context so that I am able to construct a defensible education programme within the total cash available to me which the Cabinet can approve as a whole.

Options

It is right that additional bids should be accompanied by offsetting savings (though I hope that what is said in paragraph 11 about new or increased charges will be interpreted flexibly). But I very much doubt, from past

experience, whether there is much to be gained from asking officials to produce options for reductions of 2 per cent in 1983-84 rising to 4 per cent in 1985-86. We have examined all the likely (and unlikely) candidates in recent Surveys and there is a risk that the consideration of across-the-board options in the summer will result in needlessly damaging leaks in what will be a crucial period for us politically. (This is particularly true of local authority expenditure, and we agreed with Michael Heseltine last year that, in the interests of realism, we should not in any case discuss options with the local authority associations.) I suggest that it would be much better not to ask for options in the first part of this Survey but to look at possible selective savings collectively later on in the year when we shall have details of the inescapable additional bids, a new economic assessment and the study of long term trends in expenditure to which you refer.

3. If you can reassure me on the first point and accept my suggestion on the second, I myself would not wish to raise your proposals in Cabinet on 1 April.

4. I am sending copies of this letter to the Prime Minister, the other Members of the Cabinet and Sir Robert Armstrong.

Yours.

Keith

30 MAR 1982

cc. JV
AN

FCS/82/57

CHIEF SECRETARY OF THE TREASURY

1982 Public Expenditure Survey

1. I agree that, as proposed in your recent minute to the Prime Minister, this year's Survey should be got under way and that we should aim for the time-table annexed to your minute. I wish, however, to make the following points of detail.

Options for Reductions

2. With the recollection of last year's Survey still in my mind, I am not happy with the proposition that once again Departments should cost and set out options for reductions, ranging this time from 2% to 4% of their planned expenditure. I view with dismay the prospect of a repeat of last year's exhaustive exercise, and wonder whether we really need to go through it all again? If options are considered necessary, there must be no ambiguity about their purpose. I shall put them forward entirely on an illustrative basis and without commitment. It must not be assumed that I agree to their application to any degree. I made clear last year in the context of MISC 62, and other discussions, that to close any more Diplomatic Service posts abroad would entail damage to our interests out of all proportion to the savings to be expected. You will be aware of the situation of the Aid programme from our discussions with the Prime Minister last week on India.

Manpower

3. Both wings of the FCO are on target for the agreed manpower reductions up to 1 April 1984. Further reductions could only be achieved by cutting more overseas posts or by reducing our foreign policy activiites, including Aid Administration, to an unacceptable level.

Repayment for Government Accommodation

4. My officials who have been taking part in the discussions with Treasury and PSA about the introduction of the new arrangements for Departments to bear the cost of accommodation

and services at home, are concerned about the mechanics so far proposed and, in particular, about the adequacy of the sums to be distributed to Departmental programmes. I hope that the individual requirements of Departments will be taken fully into account when the cake is sliced.

Cabinet Discussion

5. As far as my expenditure programmes are concerned, I see no need for Cabinet consideration at this stage. I note there will be further opportunities for Ministerial discussions as the Survey progresses.

6. I am sending a copy of this minute to the Prime Minister.

C

(CARRINGTON)

Foreign and Commonwealth Office
30 March 1982

1 MAR 1982

Econ Pol. Pt 19
Public Exp + cash limits

PRIME MINISTER

Statement on the Defence Estimates 1982

Leon Brittan's office have been on to me about table 2.2 in the draft Defence White Paper (at Flag A) which is for discussion at OD on Thursday.

Leon Brittan believes that the inclusion of this table, which gives comparisons in constant prices ~~in real terms~~ between defence expenditure totals in successive White Papers, is inconsistent with the move to cash planning, in precisely the way which the education figures were - and which led you to comment on Sir Keith Joseph's letter of 12 March (Flag B).

Leon Brittan further argues that inclusion of this table in its present form will lead the reader to infer that defence expenditure is planned to rise (from £13.147 billion in 1982/3 to £13.792 billion in 1984/85) slower than the 3% annual average NATO target. On this ground alone, therefore, he thinks it would be better omitted.

He wonders whether you would be prepared to authorise me to write to Defence on the lines of my letter to Education (Flag C). Agree this? If this approach is not accepted by Mr. Nott before Thursday, Leon Brittan will wish to raise the matter at OD. I understand that if he cannot secure the omission of the table, as a fall-back he will go for its inclusion on a "cost terms" basis - i.e. with the prices deflated by the GDP deflator.

MCS

30 March 1982

CONFIDENTIAL

BK

bc Mr Vereker
Econ Pol

10 DOWNING STREET

From the Private Secretary

SIR ROBERT ARMSTRONG

Public Expenditure Survey 1982

The Prime Minister last night saw your minute to Mr. Whitmore of 24 March about the timing of Cabinet discussion of the Chief Secretary's proposals for the conduct of the 1982 Public Expenditure Survey. I also had a word with her about this after OD this morning.

The Prime Minister continues to prefer 1 April rather than 6 April as the date on which the Survey would be considered by Cabinet, if discussion proves in the event necessary.

She has also given clearance - which I have passed on to the Treasury - to the circulation today of the Chief Secretary's minute to Cabinet colleagues which is aimed at securing colleagues' agreement in correspondence.

M. C. SCHOLAR

25 March 1982

CONFIDENTIAL

C cc JV AW

Prime Minister (2)

To see that this has now gone round. We now await colleagues' responses.

MCS 25/3

PRIME MINISTER

PUBLIC EXPENDITURE SURVEY 1982

As usual at this time of the year, we need to settle guidelines for the 1982 Public Expenditure Survey. The object at this stage is to enable officials to work up the material we shall need when we come to substantive discussions. My proposals are set out in the Annex to this minute.

2. In view of the need to set work in hand, I would appreciate responses from colleagues by 30 March 1982. At this stage the questions are largely procedural. But if any colleague wants a collective discussion, I understand that we could consider these proposals in Cabinet on 1 April.

3. The 1982 Survey is the first in which cash planning will be applied in full. We shall be starting with the cash plans in the White Paper just published, adjusted by the Budget changes (including the National Insurance Surcharge reductions), and by transfers of provision from the Property Services Agency in accordance with the agreed move to repayment. I propose no immediate general changes to those plans on account of new forecasts of inflation, but departmental bids can be noted where put forward for this as for other reasons. I propose that we consider again in September the prospects for inflation.

4. The 1982 Survey will take us into the mid-1980s. We shall need to reach decisions about the medium-term path of total public expenditure at which we wish to aim in the light of our general policy objectives. It would in my view be wrong simply

to extrapolate the present path of expenditure or reach decisions on a purely ad hoc basis. I will put a paper to Cabinet on this later this year. As proposed in the Chancellor's minute to you of 9 March and subsequently approved by you, officials will be considering the long-term trends in public expenditure and reporting by June.

5. I have proposed to the Ministers directly concerned some changes in the way we handle local authorities' current expenditure in the Survey. I believe these proposals offer the prospect of useful improvements compared with what happened in the 1981 Survey.

6. We shall need to consider in due course our policy for civil service manpower after 1 April 1984. At this stage, all that is necessary is to establish a baseline for the Survey which consolidates the progress we have already made and does not pre-empt further policy decisions.

7. I now seek colleagues' agreement that, as proposed in the Annex:

1. The aim should be to keep to the timetable in the Appendix to the Annex;

2. the baseline for the 1982 Survey should be the cash plans in Cmnd 8494, as modified by the Budget and agreed transfers of PSA provision, and extended to 1985-86 by adding for all programmes 4% to the 1984-85 figures, and for Defence a further 3% as well;

3. the Survey report by officials should show any additional bids for expenditure above the baseline;

4. Departments should set out, in the first instance for the Treasury and not for general circulation, offsetting savings to cover these bids and in addition fully costed options for reductions, amounting to at least 2% of the baseline in 1983-84 (starting from the uprating date for social security benefits) and 4% in 1985-86, with appropriate specified consequences for 1984-85;

5. representatives of the local authorities should be consulted about the costed options relevant to them using the machinery of the Consultative Council on Local Government Finance;

6. Manpower figures should be prepared as proposed in the Annex, in order to provide a neutral baseline for subsequent policy decisions.

8. I am sending copies of this minute to Cabinet colleagues and to Sir Robert Armstrong.

L.B.

LEON BRITTAN

CONFIDENTIAL

100 - for L.A. - Universities

ANNEX

PUBLIC EXPENDITURE SURVEY 1982

Timetable

1. It is proposed (see timetable at Appendix) that:

(i) The Ministers concerned have a preliminary look at local authority aggregate current expenditure in May (see below).

(ii) Ministers have a first look at total public expenditure and programmes in July, especially for the first year of the Survey, 1983-84.

(iii) Ministers also consider in July preliminary advice to the local authorities, and provisional figures for discussion with the nationalised industries.

(iv) Officials should clear the ground for these discussions, by consideration beforehand of Departments' bids and the scope for reductions (see below). But the main Ministerial bilaterals (covering manpower where relevant as well as expenditure) should be in the early autumn.

Prospects for inflation

2. The cash plans just published for 1983-84 and 1984-85 (adjusted by the changes announced in the Budget and by the transfer of PSA provision - see below) are the baseline for the new survey. Departments may put in bids, or offer reductions, having considered the particular circumstances of their own programmes.

3. Ministers should consider in September whether in addition to or instead of any departmental bids a general revision should be made of the plans because of changed prospects for inflation, and whether to choose and publish a separate assumption for pay in 1983-84.

4. There is no case at present for a general adjustment. The trend of inflation has been declining faster than expected last autumn. In 1981-82

price movements have been generally around, or a little less than, 11%, and wage movements mostly not far from 6%. In 1982-83 the prospects now are that 4% may be tight for pay, but other public sector price increases may be a little less than 9%. For the RPI between November 1981 and November 1982 a forecast of 9% was published with the Budget.

5. The MTFS published with the Budget shows figures for general inflation in the economy as a whole (the GDP deflator) in 1983-84 and 1984-85 of 7% and 6½%, not much higher than the cash factors used for those years in constructing the present plans. The movement in public sector costs, which include a relatively high proportion of pay, may be lower than general inflation.

6. The prospects for inflation will need to be taken into account in the consideration of preliminary guidance to the local authorities to be given in the summer.

1985-86

7. The new survey will extend to 1985-86. The 1985-86 baseline will be the same as the 1984-85 baseline figures plus, as an assumption for inflation, 4%. Any differences likely to result from "existing policies" should be costed and put forward as proposed increases or reductions, except that for Defence 3% real growth should be treated as already established policy (as recorded in Cabinet conclusions CC(81)24th Conc 18 June 1981), and incorporated in the baseline.

Local authorities' current expenditure

8. Certain improvements have been proposed in the handling of local authority relevant current expenditure, namely:

(i) the Ministers concerned should consider in May the latest information about trends in local authority aggregate expenditure, and decide whether to ask officials to study the implications for services of a change in the aggregate plans, before Cabinet consider in July preliminary advice to the local authorities;

(ii) transfers of provision from local authority relevant current expenditure, which cannot be tightly controlled, to other areas (eg

central Government) should be ruled out;

(iii) rate support grant should be planned in cash.

Additional bids and offsetting savings

9. Any bids for additions to the baseline should be accompanied by proposals for fully offsetting savings. Estimating increases on demand-determined services count as additional bids; estimating reductions, provided they are reasonably certain, as savings. Proposed savings should be listed in order of acceptability.

10. Savings on local authorities' relevant current expenditure should not be put forward as offsets to increases on other kinds of expenditure, nor in lieu of options (see below) on other expenditure.

11. New or increased charges are a legitimate method of reducing net public expenditure, but in many cases add directly to inflation or are politically sensitive. They may be suggested as possible savings, but, except where otherwise agreed with the Treasury, alternatives should also be suggested in the form of efficiency savings or cuts in services.

Options

12. Officials should set out for every programme what would be involved in reductions amounting to at least 2% of the baseline for 1983-84 rising to at least 4% of the baseline (constructed as proposed above) for 1985-86, with appropriate consequences for the intervening year 1984-85. For social security the reductions should be applied from the November uprating dates.

13. These options should be in addition to the savings proposed as offsets to additional bids. As in 1981, details will not be circulated generally. The purpose is to provide material for considering the scope for reductions in some programmes to offset possible increases in others. Efficiency savings, disposals, and the scope for switching from current expenditure to capital, should receive particular attention.

14. As in earlier years, representatives of the local authorities should be brought into discussion of options which affect them.

Manpower

15. Officials should provide information about the civil service manpower figures planned for each year. For the baseline, the figures for 1983-84 should be consistent with, or below, the agreed departmental targets for 1 April 1984; for 1984-85 and 1985-86 they should be at or below that target. Any bids for more, whether in 1983-84 (against the contingency margin for that year), or for the later years, should be put in as such and explained with reasons. This applies to all such bids, including those already discussed with the Treasury.

Government accommodation

16. In April 1983 repayment by Departments is to be introduced for PSA's expenditure on Government civil accommodation. The baseline for the 1982 survey for each Department will include a share of the White Paper provision for the PSA. Departments can then consider whether to provide, within their total programmes, more or less than that share for their accommodation needs and indicating how far any additional provision can be regarded as linked with improvements in efficiency.

APPENDIX

OUTLINE TIMETABLE FOR SURVEY

April	Departments begin to prepare bids and options.
May	Proposals on bids and options (and other draft material for PESC report) from Departments to Treasury for discussion with Treasury and other interested Departments (by 7 May).
	Ministerial consideration of local authority totals.
	Agreed material for PESC report to Treasury for circulation to Departments generally (options for reductions not to be circulated generally) by 28 May (or 4 June if Departments can provide Treasury with a fair copy of the text and a compatible tape for the Word Processor).
June	If so decided by Ministers, examination by officials of consequences of May discussion for LA services.
	Discussion at official level of bids and options for reduction.
July	Circulation of PESC report to Cabinet (2 July).
	E discussion of nationalised industries, including provisional decisions on totals.
	Cabinet discussion of: - Chancellor's paper on economic background - Chief Secretary's paper on provisional public expenditure totals (including provisional proposals on bids and cuts for each Department) and particularly recommendations on local authority totals.
Late July/August	Preliminary advice issued to local authorities and to Departments on nationalised industries.
September	Cabinet discussion of inflation provision.
	Bilaterals, covering both manpower and expenditure.
	Discussion of nationalised industries (officials) and local authorities (officials and appropriate Cabinet Committee).
October	E discussion of nationalised industries.
	Cabinet Committee discussions of local authorities.
	Cabinet discussion of: - Chancellor's paper on economic background - Chief Secretary's paper on expenditure totals and programmes.

CONFIDENTIAL

BK

10 DOWNING STREET

From the Private Secretary

25 March 1982

1982 Survey Guidelines

Thank you for your letter of 24 March to which you attached a draft minute to the Prime Minister and Cabinet colleagues on the 1982 Survey Guidelines.

The Prime Minister is content for this minute to be circulated later on today. She has also decided that, if a Cabinet discussion proves necessary, this should take place on 1 April.

M. C. SCHOLAR

Terry Mathews, Esq.,
HM Treasury

CONFIDENTIAL

(c fede hd)

Prime Minister

Mrs 25/3

Treasury Chambers, Parliament Street, SW1P 3AG

cc AW
JV

Rt Hon John Nott MP
Secretary of State
Ministry of Defence
Main Building
Whitehall
London SW1A 2HB

25 March 1982

Dear Secretary of State,

1982 PUBLIC EXPENDITURE SURVEY

I enclose a copy of a minute which I have sent to the Prime Minister, setting out my proposals for the handling of the 1982 Public Expenditure Survey. As you know, we always circulate proposals of this kind at this time in the year, so as to get the exercise off to a good start, with Cabinet backing.

The paper suggests how we might establish a baseline for the 1982 Survey by projecting the already-agreed figures for 1984-85 for one further year. In most cases we can do this mechanically, by applying a straight 4 per cent increase. In the case of the Defence Budget, there is an existing Cabinet decision which effectively decides the level of the Defence Budget in that year. This explains why I have suggested that we should treat you separately this year, rather than apply a mechanical projection which is out of line with the existing Cabinet agreement. Since this operates in your favour, I do not suppose you will object.

The paper also calls for the production of "options" from all departments. In the case of the Defence Budget, I do not think this is strictly necessary, or indeed useful. Later in the year we may have to look further at the question of the level of Defence expenditure. But at this stage, I don't think that somewhat artificial "options for reduction" will make much sense. So I do not ask you at this stage to produce "options" for the Ministry of Defence. Nor would we ask you provide "offsetting savings" for any additional bids you may make.

I am sending a copy of this letter to the Prime Minister.

Yours sincerely,

for LEON BRITTAN

Confidential (approved by the Chief Secretary & signed in his absence.)

10 DOWNING STREET

(1)

Prime Minister

(1) Leon Brittan wishes to try to clear the Public Expenditure guidelines paper (flag A) in correspondence. May he circulate to Cabinet tomorrow evening?

(2) Do you wish the Cabinet discussion, if one proves necessary, to be on 1 April or 6 April?

MCS 24/3

Ref: A07912

CONFIDENTIAL

MR. WHITMORE

Public Expenditure Survey 1982

The Prime Minister has agreed that the Chief Secretary should aim to clear in correspondence his proposals for the conduct of the 1982 Public Expenditure Survey. He will circulate a minute later this week. If, contrary to the Treasury's hopes, any Minister objects to what is proposed, the minute will have to be brought to Cabinet for discussion. The Treasury are anxious to reach conclusions before the Easter holiday so that the exercise can get under way.

2. I had hoped that it might be possible for this discussion to take place at the last Cabinet before Easter on Tuesday, 6th April. The Chancellor of the Exchequer will be in Wales that day on Royal Mint duties which he cannot cancel since they involve a visit to the Mint by the Prince of Wales. The Chancellor would have been willing for the Chief Secretary to deal with the issue in his absence, since the minute will be in the Chief Secretary's name, and he is responsible for the details of the exercise. I understand, however, that in commenting on last week's business note, the Prime Minister said that the Chancellor must be present when the Survey is discussed in Cabinet and that for this reason she was unwilling for it to be on the agenda for 6th April.

3. The only alternative Cabinet at which the Survey could be discussed is that on 1st April. There are, however, two problems about this.

4. First, we had made provision for Northern Ireland to be discussed then, following tomorrow's discussion in OD. Even if the Cabinet does not need to discuss Northern Ireland, there should be meetings of OD and MISC 7 after Cabinet on 1st April, to take the Defence White Paper and Special Nuclear Materials respectively. It would be difficult to add the Public Expenditure Survey to the Cabinet agenda without putting at risk either or both of these meetings, and both the items which they are to discuss need to be considered before Easter.

5. The second difficulty arises from the shortage of time between the circulation of the Survey memorandum and Cabinet on 1st April. Mr. Scholar's minute of 17th March recorded the Prime Minister's wish for some time to elapse before the circulation of the Chief Secretary's minute. His office are to consult yours before circulation later this week. This will leave very little time for Departments to digest the memorandum and we will not know until 30th or 31st March whether it can be cleared in correspondence or whether it has to go to Cabinet. I wonder, therefore, whether the Prime Minister might be prepared to reconsider her view that the Public Expenditure Survey should not be considered by Cabinet (if this proves necessary) in the absence of the Chancellor of the Exchequer on 6th April.

RGA

Robert Armstrong

24th March 1982

010

CONFIDENTIAL

Treasury Chambers, Parliament Street, SWIP 3AG

24th March 1982

Michael Scholar Esq
10 Downing Street

Dear Michael,

1982 SURVEY GUIDELINES

Attach is the draft minute which the Chief Secretary would like to send to the Prime Minister and Cabinet colleagues. It is his intention to exempt Defence from the "options" exercise, but to write separately to Mr Nott about this.

If you agree, the minute could, with advantage, issue on Thursday evening.

Yours sincerely

Terry Matthews

DRAFT OF CHIEF SECRETARY'S MINUTE TO PRIME MINISTER

PUBLIC EXPENDITURE SURVEY 1982

cc Members of Cabinet
Sir Robert Armstrong

1. As usu al at this time of the year, we need to ~~agree~~ settle guidelines for the 1982 Public Expenditure Survey. The object at this stage is to enable officials to work up the material we shall need when we come to substantive discussions. 2. In view of the need to set work in hand, I would appreciate responses from colleagues by 2 April 1982. At this stage the ~~problems~~ questions are largely procedural. But if any colleague wants a collective discussion, We could consider these proposals in Cabinet.

2. My proposals are set out in the Annex to this minute

3. The 1982 Survey is the first in which cash planning will be applied in full. We shall be starting with the cash plans in the White Paper just published, adjusted by the Budget changes (including the National Insurance Surcharge reductions), and by transfers of provision from the Property Services Agency in accordance with the agreed move to repayment. I propose no immediate general changes to those plans on account of new forecasts of inflation, but departmental bids can be noted where put forward for this as for other reasons. I propose that we consider again in September the prospects for inflation.

4. The 1982 Survey will take us into the mid-1980s. We shall need to reach decisions about the medium-term path of total public expenditure at which we wish to aim in the light of our general policy objectives. It would in my view be wrong simply to extrapolate the present path of expenditure or reach decisions on a purely ad hoc basis. I will put a paper to Cabinet on the later this year. As proposed in the Chancellor's minute to you of 9 March and subsequently approved by you, officials will be considering the long-term trends in public expenditure and reporting by June.

5. I have proposed to the Ministers directly concerned some changes in the way we handle local authorities' current expenditure in the Survey. I believe these proposals offer the prospect of useful improvements compared with what happened in the 1981 Survey.

6. We shall need to consider in due course ~~what~~ our policy for civil service manpower ~~should be~~ after 1 April 1984. At this stage, all that is necessary is

to establish a baseline for the Survey which consolidates the progress we have already made and does not pre-empt further policy decisions.

7. I now seek colleagues' agreement that, as proposed in the Annex:

1. The aim should be to keep to the timetable in the Appendix to the Annex;

2. the baseline for the 1982 Survey should be the cash plans in Cmnd 8494, as modified by the Budget and agreed transfers of PSA provision, and extended to 1985-86 by adding for all programmes 4% to the 1984-85 figures, and for Defence a further 3% as well;

3. the Survey report by officials should show any additional bids for expenditure above the baseline;

4. Departments should set out, in the first instance for the Treasury and not for general circulation, offsetting savings to cover these bids and in addition fully costed options for reductions, amounting to at least 2% of the baseline in 1983-84 (starting from the uprating date for social security benefits) and 4% in 1985-86, with appropriate specified consequences for 1984-85;

5. representatives of the local authorities should be consulted about the costed options relevant to them using the machinery of the Consultative Council on Local Government Finance;

6. Manpower figures should be prepared as proposed in the Annex, in order to provide a neutral baseline for subsequent policy decisions.

A

ANNEX

PUBLIC EXPENDITURE SURVEY 1982

Timetable

1. It is proposed (see timetable at Appendix) that:

(i) The Ministers concerned have a preliminary look at local authority aggregate current expenditure in May (see below).

(ii) Ministers have a first look at total public expenditure and programmes in July, especially for the first year of the Survey, 1983-84.

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From: E A Doggett GEA1
22 March 1982

MR SCHOLAR

cc Mr Mountfield
Mr Ward
Mr Rayner

RATIOS TO GDP

We provided last week a series of public expenditure/gdp ratios, and you asked whether anything could be done about the discontinuity between 1974-75 and 1975-76 resulting from the exclusion of nationalised industries market and overseas borrowing. We have now managed to make consistent estimates and the corrected figures are shown on the attached table. In view of the degree of estimation in earlier years and the possibility of revision to the later year figures I recommend that the rounded figures should be quoted.

2. I should point out that the Central Statistical Office are currently producing their estimates for the final quarter of 1981 which may lead to revisions for earlier years.

E A DOGGETT

GENERAL GOVERNMENT EXPENDITURE

at current prices

	% GDP	Rounded
1971	41.0	41
1972	41.5	41½
1973	41.8	42
1974	47.2	47
1975	49.2	49
1976	46.9	47
1977	43.0	43
1978	43.6	43½
1979	44.2	44
1980	46.0	46
1981		

PUBLIC EXPENDITURE(1)

at current prices

	% GDP	Rounded
1971-72	37.8	38
1972-73	38.9	39
1973-74	40.8	41
1974-75	46.2	46
1975-76	46.2	46
1976-77	44.5	44½
1977-78	40.3	40½
1978-79	41.2	41
1979-80	41.0	41
1980-81	43.4	43½
1981-82	44.8(2)	45
1982-83	44.3(2)	44½

(1) Public expenditure ie public expenditure planning total plus net debt interest, capital consumption, local authority VAT payments and market and overseas borrowing of nationalised industries. Market and overseas borrowing of nationalised industries for 1971-72 to 1974-75 is estimated.

(2) Estimate from Financial Statement and Budget Report 1982-83 (HC 237)

23 MAR 1982

Econ Pol

Econ Pol

10 DOWNING STREET

From the Private Secretary

SIR ROBERT ARMSTRONG

Public Expenditure Survey 1982

You minuted Mr. Whitmore on 16 March about the Treasury's wish to make progress with the 1982 Public Expenditure Survey.

The Prime Minister wishes to leave a week or two between the Budget and this new exercise. She would accordingly prefer no paper to be circulated for the time being. I have suggested to the Chief Secretary's Office that they check with me on, say, 26 March, about the circulation of their paper. I hope that this will leave enough time for the Treasury's plan to clear the paper by correspondence and - as envisaged in paragraph 3 of your minute - if this proves impossible to lay on a discussion in Cabinet without too much delay.

E E SCHOLAR

17 March 1982

Downgraded in the Secretary of States office

~~Serial No 1050 Copy No 11 of 25 Copies~~

~~SECRET~~

CONFIDENTIAL

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

Econ Pol.

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

NBPM

17 March 1982

Dear Geoffrey

LONG TERM PUBLIC EXPENDITURE PROSPECTS

I welcome the review of long-term public expenditure prospects which you have proposed in your minute of 8 March to the Prime Minister. This should provide a basis for a timely review of our priorities.

My officials will be ready to play their part in this work.

Copies of this letter go to those who received your minute.

Yours

David

DAVID HOWELL

CONFIDENTIAL

~~SECRET~~

17 MAR 1982

1

cc PSU

Prime Minister

Content for the Treasury to try to clear the paper by correspondence?

AGW 16 Mar

Ref. A07815

MR WHITMORE

Public Expenditure Survey 1982

As you know, the Prime Minister decided she would prefer not to take the Cabinet paper on this subject this week.

2. The Treasury are anxious to make progress with the discussion of this subject; they need early decisions, largely from the point of the view of the local authority programmes. They believe that their proposals are unlikely to be contentious (but they could be wrong about that: some of the Prime Minister's colleagues will not take kindly to another "options cuts" exercise). They have suggested that we might see if it is possible to clear the paper by correspondence.

3. I do not think that we have anything to lose by this. If the Treasury are right in thinking that the paper is uncontentious, we shall have saved ourselves a discussion; if it is contentious and a discussion is demanded, we shall have some idea of the nature and extent of the objections to the Treasury proposals.

4. If the Prime Minister agrees, I should like to invite the Treasury to seek to clear the paper in correspondence, at any rate in the first instance.

I would still leave a week or two between the Budget and this new exercise

RTA

ROBERT ARMSTRONG

16 March 1982

SECRET

File

cc: Cabinet
CWO
CO

10 DOWNING STREET

bcc: John Vereker

From the Private Secretary

16 March 1982

LONG TERM PUBLIC EXPENDITURE PROSPECTS

The Prime Minister was grateful for the Chancellor's minute of 8 March, in which he proposed a study of the likely pattern of public expenditure over the next decade.

The Prime Minister is content with the proposals set out in paragraph 7 of the Chancellor's minute.

I am sending copies of this letter to the Private Secretaries to the other members of Cabinet, to Murdo Maclean (Chief Whip's Office) and David Wright (Cabinet Office).

M. C. SCHOLAR

John Kerr, Esq.,
H. M. Treasury.

SECRET

File 2 bc: John Vereker

10 DOWNING STREET

From the Private Secretary

16 March 1982

Dear Imogen,

DRAFT PAPER FOR EXPENDITURE STEERING GROUP - EDUCATION

The Prime Minister has been following the correspondence between your Secretary of State and the Chief Secretary about the presentation in cash or in real terms of figures for education expenditure in this paper.

The Prime Minister considers that your Department's proposals in this regard put in question the primacy of cash planning. In relation to the proposal, in paragraph 2(c) of your Secretary of State's letter of 12 March, she has minuted that the Government wishes to get away from the presentation in "real" terms; and that this was always an artificial concept.

I am sending copies of this letter to Terry Mathews (Chief Secretary's Office) and to David Wright (Cabinet Office).

Yours sincerely,

Michael Scholar

Mrs. Imogen Wilde,
Department of Education and Science.

Econ Pol

cc Mr Walters
Mr Gregson, CO

10 DOWNING STREET

From the Private Secretary

15 March 1982

Thank you for your letter of 12 March with which you enclosed a draft paper for Cabinet proposing guidelines for the 1982 Public Expenditure Survey.

The Prime Minister would prefer to defer Cabinet discussion of this matter for three weeks or so. On present plans, therefore, it might be taken at Cabinet on Tuesday, 6 April.

M. C. SCHOLAR

Terry Mathews Esq
Chief Secretary's Office.

CONFIDENTIAL

Prime Minister (2)

MCS 15/3 c JC

DEPARTMENT OF EDUCATION AND SCIENCE

ELIZABETH HOUSE, YORK ROAD, LONDON SE1 7PH

TELEPHONE 01-928 9222

FROM THE SECRETARY OF STATE

12 March 1982

The Rt Hon Leon Brittan QC MP
Chief Secretary
HM Treasury
Whitehall
London SW1

They are disputing cash planning!

MT

MT

Dear Chief Secretary,

DRAFT PAPER FOR EXPENDITURE STEERING GROUP - EDUCATION

When we spoke last night we agreed that officials should try to reach agreement today about amendments to this paper. I made it clear that I was not disputing the primacy of cash planning and you said that you would ask Treasury officials to look again at the drafting and figures so as to meet me part of the way. ?

2 I understand that at a meeting this morning officials came close to agreement on amendments to the paper which would have (a) emphasised still more strongly than in paragraph 4 of the previous draft the primacy of cash, (b) inserted a new table in cash before the present table in paragraph 7 and (c) substituted for that table another showing the implications in real terms (on specified assumptions about pay and prices) for each sub-programme of the cash table not in £ but by index numbers, ie 1980-81 = 100, 1982-83 = 96.1, 1983-84 = 92.8.

But we want to get away from real terms. It was always an artificial concept.

3 I shall be grateful if you will let me know by mid-day on Monday that you can agree to this so that we can circulate the paper in time for Friday's meeting of ESGE. Otherwise I shall have to agree to the postponement of the meeting. This would mean a loss of momentum in following up the Public Expenditure White Paper. Over most of the education programme our policy calls for contraction which will not come about by itself and will not be brought about unless the detailed practical implications are clearly explained and driven home in good time to local authorities. They have co-operated with successive governments in their plans for educational spending, and I would not wish to damage the machinery which has served us well for several years.

4 I am sending copies of this letter to the Prime Minister and Sir Robert Armstrong.

Yours sincerely,

Imogen Wilde

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

CONFIDENTIAL

2 MAR 1996

It is too soon in my view to bring this paper before Cabinet. Wait for 3 or so weeks.

10 DOWNING STREET

(1)

Prime Minister

Leon Brittan's Public Expenditure paper

(1) Please see Peter Gregson's note at flag A, recommending that this paper be taken at next Thursday's Cabinet.

(2) I am sure this is right. But I think Peter underestimates John Nott's likely hostility – particularly on the proposal that there should be 2% - 4% costed options for defence (as for every other programme)

(3) Please see Mrs. Alan's note at

OVER

Flag B. I am not sure about his second suggestion: the idea is to assemble a menu of reductions in expenditure across the board – so that the Cabinet can pick and choose between them.

(4) Agree to circulation of this paper?

(5) May John Hoskyns and Alan Walters attend the Cabinet meeting?

MCS 12/3

cc AW
JV

Treasury Chambers, Parliament Street, SW1P 3AG

Michael Scholar Esq
No. 10 Downing Street
London SW1

12 Marcn 1982

Dear Michael

Cabinet next Thursday will be discussing the subject of the 1982 Public Expenditure Survey guidelines.

The Chief Secretary, with the Chancellor of the Exchequer's agreement, is proposing to circulate the attached paper as a basis for discussion. I should be grateful if you could let me know quickly whether the Prime Minister is content for the paper to be circulated.

Yours sincerely

Terry Mathews

T F MATHEWS

Private Secretary

DRAFT OF CHIEF SECRETARY'S PAPER FOR CABINET PUBLIC EXPENDITURE SURVEY 1982: GUIDELINES

Memorandum by the Chief Secretary

1. This paper proposes guidelines for the 1982 Public Expenditure Survey which require collective Ministerial agreement. The object at this stage is as usual to enable officials to work up the material we shall need when we come to substantive discussions.

2. My proposals are set out in the Annex.

3. The 1982 Survey is the first in which cash planning will be applied in full. We shall be starting with the cash plans in the White Paper just published, adjusted by the Budget changes (including the National Insurance Surcharge reductions), and by transfers of provision from the Property Services Agency in accordance with the agreed move to repayment. I propose no immediate general changes to those plans on account of new forecasts of inflation, but departmental bids can be noted where put forward for this as for other reasons. I propose that we consider again in September the prospects for inflation.

4. The 1982 Survey will take us into the mid-1980s. We shall need to reach decisions about the medium-term path of total public expenditure at which we wish to aim in the light of our general policy objectives. It would in my view be wrong simply to extrapolate the present path of expenditure or reach decisions on a purely ad hoc basis. I will put a paper to Cabinet later this year.

privately, * in fact, the position is: you agreed, to the Chancellor's proposal for this study. He is now launching the proposal on colleagues. MCS 11/3

As proposed in the Chancellor's minute* of 8 March to the Prime Minister, [and subsequently approved by her] officials will be considering the long-term trends in public expenditure and reporting by June.

5. I have proposed to the Ministers directly concerned some changes in the way we handle local authorities' current expenditure in the Survey. I believe these proposals offer the prospect of useful improvements compared with what happened in the 1981 Survey.

6. We shall need to consider in due course what our policy for Civil Service manpower should be after 1 April 1984. At this stage, all that is necessary is to establish a baseline for the Survey which consolidates the progress we have already made but does not pre-empt further policy decisions.

7. I now seek colleagues' agreement that, as proposed in the Annex.

1) the aim should be to keep to the timetable in the Appendix to the Annex;

2) the baseline for the 1982 Survey should be the cash plans in Cmnd 8494, as modified by the Budget and agreed transfers of PSA provision, and extended to 1985-86 by adding 4% to the 1984-85 figures, and for Defence a further 3%;

3) the Survey report by officials should show, alongside any additional bids, fully offsetting savings; and, in addition, costed policy options for reductions amounting to at least 2% of the baseline in 1983-84 (starting from the uprating date in the case of social security benefits) and 4% in 1985-86 with appropriate specified consequences for 1984-85.

4) representatives of the local authorities should be consulted about the costed options relevant to them, using the machinery of the Consultative Council on Local Government Finance;

5) manpower figures should be prepared as proposed in the Annex in order to provide a neutral baseline for subsequent policy decisions.

PUBLIC EXPENDITURE SURVEY 1982

Timetable

1. It is proposed (see timetable at Appendix) that:-

i) The Ministers concerned have a preliminary look at local authority aggregate current expenditure in May (see below).

ii) Ministers have a first look at total public expenditure and programmes in July, especially for the first year of the Survey, 1983-84.

iii) Ministers also consider in July preliminary advice to the local authorities, and provisional figures for discussion with the nationalised industries.

iv) Officials should clear the ground for these discussions, by consideration beforehand of Departments' bids and the scope for reductions (see below). But the main Ministerial bilaterals (covering manpower where relevant as well as expenditure) should be in the early autumn.

Prospects for inflation

2. The cash plans just published for 1983-84 and 1984-85 (adjusted by the changes announced in the Budget and by the transfer of PSA provision -see below) are the baseline for

the new survey. Departments may put in bids, or offer reductions, having considered the particular circumstances of their own programmes.

3. Ministers should consider in September whether in addition to or instead of any departmental bids a general revision should be made of the plans because of changed prospects for inflation, and whether to choose and publish a separate assumption for pay in 1983-84.

4. There is no case at present for a general adjustment. The trend of inflation has been declining, faster than expected last autumn. In 1981-82 price movements have been generally around, or a little less than, 11%, and wage movements mostly not far from 6%. In 1982-83 the prospects now are that 4% may be tight for pay, but other public sector price increases may be a little less than 9%. For the RPI between November 1981 and November 1982 a forecast of 9% was published with the Budget.

5. The MTFS published with the Budget shows figures for general inflation in the economy as a whole (the GDP deflator) in 1983-84 and 1984-85 of 7% and 6½%, not much higher than the cash factors used for those years in constructing the present plans. The movement in public sector costs, which include a relatively high proportion of pay, may be lower than general inflation.

6. The prospects for inflation will need to be taken into account in the consideration of preliminary guidance to the local authorities to be given in the summer.

1985-86

7. The new survey will extend to 1985-86. The 1985-86 baseline will be the same as the 1984-85 baseline figures plus, as an assumption for inflation, 4%. Any differences likely to result from "existing policies" should be costed and put forward as proposed increases or reductions, except that for Defence 3% real growth should be treated as already established policy, and incorporated in the baseline.

Local authorities' current expenditure

8. Certain improvements have been proposed in the handling of local authority relevant current expenditure, namely:

i) the Ministers concerned should consider in May the latest information about trends in local authority aggregate expenditure, and decide whether to ask officials to study the implications for services of a change in the aggregate plans, before Cabinet consider in July preliminary advice to the local authorities;

ii) transfers of provision from local authority relevant current expenditure, which cannot be tightly controlled, to other areas (eg central Government) should be ruled out ;

iii) rate support grant should be planned in cash.

Additional bids and offsetting savings

9. Any bids for additions to the baseline should be accompanied by proposals for fully offsetting savings. Estimating increases on demand-determined services count as additional bids; estimating reductions, provided they are reasonably certain, as savings. Proposed savings should be listed in order of acceptability.

10. Savings on local authorities' relevant current expenditure should not be put forward as offsets to increases on other kinds of expenditure, nor in lieu of options (see below) on other expenditure.

11. New or increased charges are a legitimate method of reducing net public expenditure, but in many cases add directly to inflation or are politically sensitive. They may be suggested as possible savings, but, except where otherwise agreed with the Treasury, alternatives should also be suggested in the form of efficiency savings or cuts in services

Options

12. Officials should set out for every programme what would be involved in reductions amounting to at least 2% of the baseline for 1983-84 rising to at least 4% of the baseline (constructed as proposed above) for 1985-86, with appropriate consequences for the intervening year 1984-85. For social security the reductions should be applied from the November uprating dates.

13. These options should be in addition to the savings proposed as offsets to additional bids. As in 1981, details will not be circulated generally. The purpose is to provide material for considering the scope for reductions in some programmes to offset possible increases in others. Efficiency savings, disposals, and the scope for switching from current expenditure to capital, should receive particular attention.

14. As in earlier years, representatives of the local authorities should be brought into discussion of options which affect them.

Manpower

15. Officials should provide information about the Civil Service manpower figures planned for each year. For the baseline, the figures for 1983-84 should be consistent with, or below the agreed departmental targets for 1 April 1984; for 1984-85 and 1985-86 they should be at or below that target. Any bids for more, whether in 1983-84 (against the contingency margin for that year) or for the later years, should be put in as such and explained with reasons. This applies to all such bids, including those already discussed with the Treasury.

Government accommodation

16. In April 1983 repayment by Departments is to be introduced for PSA's expenditure on Government civil accommodation. The baseline for the 1982 survey for each Department will include a share of the White Paper provision for the PSA. Departments can then consider whether to provide, within their total programmes, more or less than that share for their accommodation needs, and indicating how far any additional provision can be regarded as linked with improvements in efficiency.

OUTLINE TIMETABLE FOR SURVEY

March	Departments begin to prepare bids and options.
April	Proposals on bids and options (and other draft material for PESC report) from Departments to Treasury for discussion with Treasury and other interested Departments (by 30 April).
May	Ministerial consideration of local authority totals.
June	Agreed material for PESC report to Treasury for circulation to Departments generally (options for reductions not to be circulated generally) (4 June). If so decided by Ministers, examination by officials of consequences of May discussion for LA services. Discussion at official level of bids and options for reduction.
July	Circulation of PESC report to Cabinet (2 July). E discussion of nationalised industries, including provisional decisions on totals. Cabinet discussion of:- - Chancellor's paper on ~~macro-economy~~ economic background. - Chief Secretary's paper on provisional public expenditure totals (including provisional proposals on bids and cuts for each Department) and particularly recommendations on local authority totals.
Late July/August	Preliminary advice issued to local authorities and to Departments on nationalised industries.
September	Cabinet discussion of inflation provision. Bilaterals, covering both manpower and expenditure. Discussion of nationalised industries (officials) and local authorities (officials and appropriate Cabinet Committee).
October	E discussion of nationalised industries. Cabinet Committee discussions of local authorities. Cabinet discussion of:- - Chancellor's paper on ~~macro-economy~~ economic background. - Chief Secretary's paper on expenditure totals and programmes

cc JU
BW

2 pps

P.0678

MR SCHOLAR

cc Mr Wright
Mr Moore

PUBLIC EXPENDITURE SURVEY 1982: GUIDELINES

You asked for advice on the letter from the Chief Secretary's office of 12 March addressed to you covering a draft paper on the guidelines for the Public Expenditure Survey 1982 and seeking the Prime Minister's agreement to the circulation of the paper to the Cabinet.

2. It had been provisionally arranged that this paper should come to the Cabinet on 18 March. Until a few days ago it was thought that there would be a paper at the same meeting on End-Year Flexibility. It was known that this matter was of particular interest to the Secretary of State for Defence and it was thought that he might be less likely to raise objections to the proposals for the Public Expenditure Survey guidelines if he had received some satisfaction on End-Year Flexibility.

Treasury and MOD have not yet been able to agree on an End-year Flexibility paper.

MCS

3. I have therefore investigated the following points:

i. How far the absence of a paper on End-Year Flexibility on 18 March is likely to cause Mr Nott to be difficult about the PES guidelines paper.

ii. Whether the absence of the End-Year Flexibility paper is likely to cause problems with other Ministers.

iii. How far the proposals in the PES guidelines paper are likely to be contentious with Mr Nott or with Ministers generally.

iv. How important it is to have the PES guidelines paper approved on 18 March.

4. On i. I understand that Treasury and MoD officials are working on arrangements to ensure that there is no problem over the defence budget at the end of this financial year. It is thought that a solution can be found to the projected underspend in this year and overspend next year by some adjustment of billing dates. Mr Nott knows that this is going on and the belief is that he will therefore not complain on 18 March that there are no proposals before the Cabinet on End-Year Flexibility in general. He will of course be concerned that the Cabinet should consider the general issue in due course but he is not thought likely to raise difficulties on 18 March.

5. On ii. there is no reason to think that the attitude of Ministers other than Mr Nott on 18 March is likely to be affected significantly by the absence of the End-Year Flexibility paper. They will know from their officials that work is going on and they should be content that proposals will come forward in due course. If the matter is raised the Chief Secretary will be able to explain that End-Year Flexibility is not relevant to the setting in motion of the Public Expenditure Survey work. It could be important when the final expenditure decisions have to be taken in the autumn, but the matter should have been dealt with well before then.

No - he will be intensely suspicious of the Treasury paper MCS

6. On iii. there is no reason to think that the PES guidelines paper will be particularly contentious for Mr Nott or for other Ministers. As far as Mr Nott is concerned the Treasury considers that it has dealt with his major concern by the proposal in 7(2) of the paper that the defence budget should have an extra 3 per cent added in 1985-86. If there is difficulty it is likely to arise on two issues: the question of whether there should be an "options" exercise, and the adequacy of the inflation assumptions. On the "options" exercise the Treasury will explain that this exercise does not pre-judge the issue of whether there will be expenditure cuts; the intention is to provide some scope for considering off-setting savings when additional bids are proposed. Mr Nott might argue that he should be exempt from the "options" exercise but it is thought on balance that it is more likely that that argument will take place later in the year. On the

but does Mr Nott?

I doubt it MCS

inflation assumptions the annex to the paper makes it clear (paragraph 3) that the case for revision of the inflation assumptions will be considered by Ministers in September. In any event the inflation assumptions published in the MTFS are not much higher than the cash factors currently being used.

7. On iv. the Treasury is very keen to get the Survey under way so that Ministers can have sensible discussions in July. It is true that the guidelines paper was not taken by the Cabinet last year until the beginning of May but the Survey was not handled satisfactorily last year. There is particular concern this year to deal with local authority expenditure more satisfactorily and some new procedures have been built in for this purpose. If the guidelines paper were to be deferred until a paper could be discussed on End-Year Flexibility, this would mean postponement until after the Easter recess and the timetable would slip by at least a month.

8. In the light of all this there seems to be a good case for agreeing to the circulation of the Chief Secretary's paper on the PES guidelines for discussion by the Cabinet on 18 March.

PG

P L GREGSON

12 March 1982

2 MAR 1982

cc Mr. Hoskyns
Mr. Vereker

MR. SCHOLAR

PUBLIC EXPENDITURE SURVEY 1982: GUIDELINES

Although I am not sure how far the Chief Secretary needs to go in this paper for Cabinet, I think it is worth while at this stage or some other stage bearing in mind the following points.

1. Cabinet and E have, rightly in my view, laid very considerable emphasis on the distinction between on the one hand expenditure on direct employment and on the other hand expenditure on contracts with the private sector - mainly of course investment expenditure. I should have thought this distinction needs to be made quite centrally in all the preparations.

2. As usual, the survey calls for optional cuts of 2% of the base line in 1983/84 and 4% in 1985/86. Is it not appropriate at this stage, even before the long term review of public spending, to take a rather more bold line? Should we not identify programmes that ought to be reduced? This would differ considerably according to departments. What I am looking for is a really positive approach to reducing public spending, not merely the 2% chipping away across the board. This of course requires political decisions, but someone should be taking those issues on board. Otherwise its simply a case of Perm Secs rule OK?

3. As an illustration, in the 20 years from 1960-1980 the total staff in the Health Service has more than doubled, from 565,000 to 1,228,000 (source Hansard 1 December 1981 column 88). Yet the number of people covered has increased by less than 1%. And waiting lists have grown. And the growth continues at some 24,000 over 1979-80.

AW

12 March 1982

ALAN WALTERS

PART 18 ends:-

s/s DES to CST + att of 10/3/82

PART 19 begins:-

Ltr to MCS of 12/3/82

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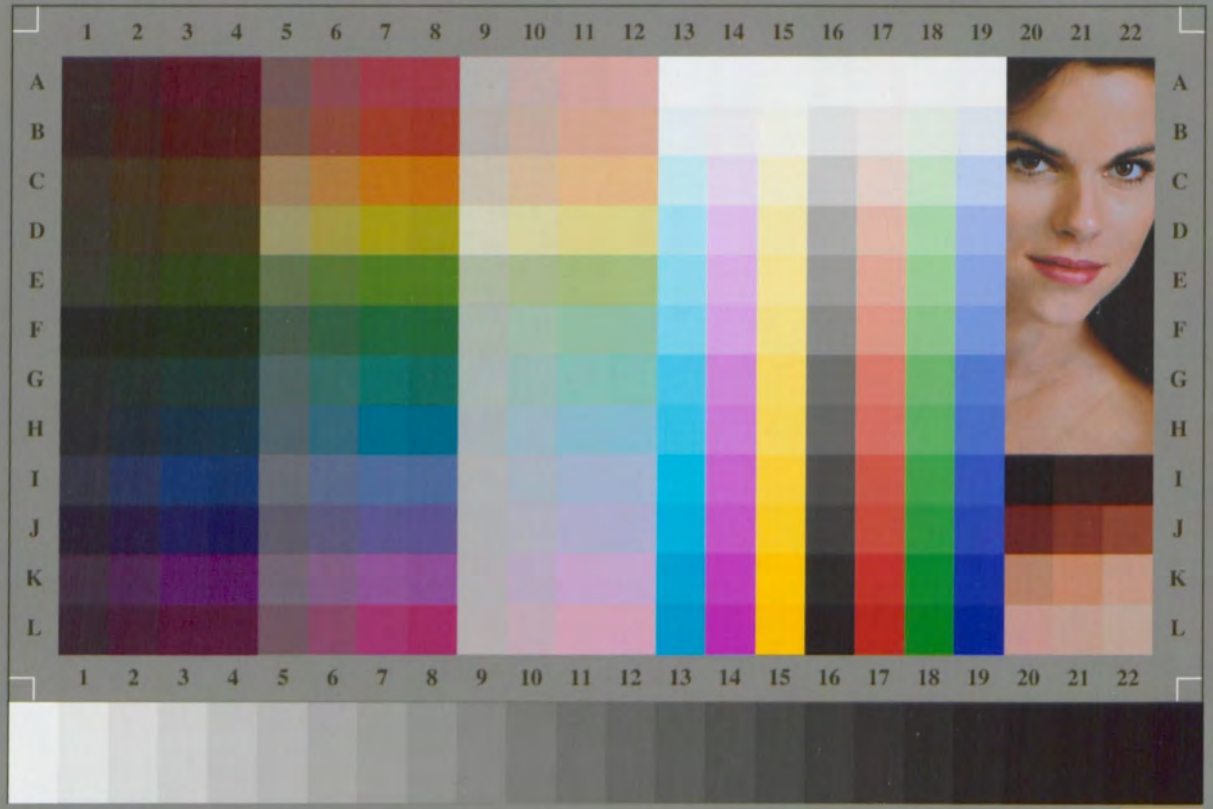

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