PREM 19/983

Public Expenditure + Cash Limits

ECONOMIC POLICY

Part 1: May 1979

Part 21: Oct 1982

PART 21

Referred to	Date	Referred to	Date	Referred to	Date	Referred to	Date
~~1.10.82~~		~~29.3.83~~					
~~11.10.82~~		~~6.4.83~~					
~~14.10.82~~		24.1.83					
~~22.10.82~~							
1.11.82							
~~2.11.82.~~							
~~5.11.82~~							
~~8.11.82~~							
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~~15.12.82~~							
~~16.12.82.~~							
~~17.12.82.~~							
~~30.12.82~~							
~~21.1.83~~							
~~24.1.83~~							
~~1.2.83.~~							
~~4.2.83.~~							
~~16.3.83~~							
~~21.3.83~~							

PREM 19/983

PART 21 ends:-

MCS to CST's office 24.1.83.

PART 22 begins:-

RTA to MCS (A083/0246) 24.1.83

TO BE RETAINED AS TOP ENCLOSURE

Cabinet / Cabinet Committee Documents

Reference	Date
MISC 21 (82) 1st Meeting, Minutes	21.10.82
C(82) 38	29.10.82
CC(82) 46th Meeting, Minute 2, with Limited Circulation Annex	2.11.82

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 D Wayland Date 13 March 2013

PREM Records Team

Published Papers

The following published paper(s) enclosed on this file have been removed and destroyed. Copies may be found elsewhere in The National Archives.

1. HM Treasury Autumn Statement 1982
HMSO, November 1982 (ISBN 010 201083 8)

2. Cmnd. 8775: Public Expenditure on the Social Services
HMSO (ISBN 010 187750 1)

3. Governments' Expenditure Plans, 1983-84 to 1985-86, Volumes 1 and 2
HMSO, February 1983 (Cmnd 8789-I and 8789-II)

Signed CWayland Date 13 March 2013

PREM Records Team

File

Econ Pol
Pub Exp Pt 21
with PCO

bc: Mr. Ingham

10 DOWNING STREET

From the Private Secretary

24 January 1983

PUBLICATION OF 1983 PUBLIC EXPENDITURE WHITE PAPER

Thank you for your letter of 21 January, which I showed the Prime Minister over the weekend.

Mrs. Thatcher agrees to your publishing the White Paper on 1 February, but would prefer that, in line with present practice, the White Paper should be published at 3.30 p.m. on that day, with advance copies made available under embargo at noon for the convenience of journalists. The Prime Minister is otherwise content with the arrangements set out in your letter. She has asked that the Treasury, in making its arrangements for publication, consult and agree these, in the usual way, with the Press Office here at Downing Street.

I am sending a copy of this letter to David Heyhoe (Lord President's Office).

M. C. SCHOLAR

John Gieve, Esq.,
Chief Secretary's Office,
H.M. Treasury.

PRIME MINISTER

1983 PUBLIC EXPENDITURE WHITE PAPER - EMBARGO

The attached letter from the Treasury on their proposals for publication of the 1983 Public Expenditure White Paper should be read against my argument with Jock Bruce-Gardyne over the embargo system in your room last week.

The effect of the Treasury letter is to try unilaterally to overthrow the restrictive policy the Government adopted, with your approval, after the wholesale breach of the Falklands Honours embargo.

Essentially what the Treasury are proposing for the publication of the Public Expenditure White Paper on February 1 is a return to the old system of 24-hour overnight embargoes.

I hope I can rely on your support to block this move.

There is no doubt that my information colleagues and I wish to return to a more flexible embargo system as soon as we can have confidence to do so. The Press Council judgement, as you know, has given us no cause for confidence because its effect is positively to encourage journalists to break embargoes.

However, I think we could have some confidence in returning to a more flexible embargo regime on the basis of the replies I have received to my letter of last October from the BBC, IBA, Newspaper Society, Newspaper Conference, the Guild of British Newspaper Editors, the Scottish Daily Newspaper Society and the Press Association.

Unfortunately the Newspaper Publishers' Association, the organisation representing all bar one of the prime offenders, has taken three months to reply to my letter. And its reply goes no further than suggesting that the matter could best be progressed by an informal lunch or meeting. I am pressing them for a written assurance.

/This is not ....

This is not therefore the time for the Government to show weakness which the Treasury move, if allowed, would manifest. I hope you agree we must maintain a firm and resolute negotiating position.

I should add that the House would be severely critical of you if, without an agreement from the Newspaper Publishers' Association, Fleet Street were to break an embargo on a Command or Parliamentary paper under a more relaxed embargo regime.

Content that, in line with present practice, the Treasury should be told that the 1983 Public Expenditure White Paper should be published at 3.30pm on February 1, with advance copies made available under embargo at noon for the convenience of journalists?

B. INGHAM
21 January 1983

Yes - I am in total agreement with Bernard

MT

52

Romola

Comments pl by MS

evening

MCS 21/1

CHIEF SECRETARY TO THE TREASURY

Treasury Chambers, Parliament Street, SW1P 3AG

M C Scholar Esq
Private Secretary to the
Prime Minister
No. 10 Downing Street
London SW1

21 January 1983

Dear Michael,

PUBLICATION OF 1983 PUBLIC EXPENDITURE WHITE PAPER

The preparation of the 1983 White Paper is on schedule, and we expect to have it ready on 31 January as planned. An oral statement in the House on publication of the White Paper does not seem necessary on this occasion, particularly as the White Paper will no doubt be followed by a fairly early debate. It should be sufficient to announce the date and time of publication in a Written answer and then place copies in the Vote Office. It would help with the publicity arrangements if the Answer could be given on Monday 31 January saying that copies of the White Paper would be available at 10 am on the following day. If the Prime Minister is content the Chief Secretary therefore proposes that publication should be on Tuesday 1 February. Our consultations show that this would not clash with any other major publication or announcement.

The Chief Secretary proposes to take an on-the-record press conference on the White Paper from 10.30 to 11.15 am on Tuesday 1 February.

The White Paper is a long and complex document, and we propose to issue Confidential Final Revises (CFRs) on the afternoon of Monday 31 January, embargoed until 10.00 am on the following day. An overnight embargo would not only help journalists in the preparation of their articles; it would also give us a better prospect of balanced and considered coverage in the press, and more opportunity to influence that coverage. This is particularly important given current sensitivities on the exchange rate. We will not require more than the 200 copies of CFRs normally allowed, but we do wish to provide copies to the economic and financial correspondents who usually write on public expenditure topics and have received CFRs in the past, and I shall be grateful for the approval of your Press Office to our doing this.

It would be helpful if you could let me have a decision by Monday 24 January so that our publicity arrangements can be finalised.

I am sending a copy to David Heyhoe.

yours sincerely

for JOHN GIEVE

Econ Pol, Public Expenditure, Pt 21

21 JAN 1982

SECRET

11 c/c JV (2)

Prime Minister

MCS 21/12

PRIME MINISTER

LONG-TERM PUBLIC EXPENDITURE: EDUCATION

I regret to say that the figures which ~~were~~ I used in the meeting with you, the Chancellor and the Chief Secretary about expenditure prospects last Wednesday - figures reported correctly in your Private Secretary's letter of 15 December - related to proposals more ambitious than those which I am in fact about to propose to colleagues.

2 The proposals that I am making involve savings of about £250m fructifying in about fifteen years with a short term increase of expenditure in the early years rising to as much as £60m depending upon the details finally agreed.

3 I shall be discussing the proposals with the Chancellor and the Chief Secretary at a meeting arranged for 12 January and shall then be putting them to H Committee as soon as possible thereafter.

4 I am copying this minute to the recipients of Michael Scholar's letter of 15 December to Imogen Wilde.

KJ

21 December 1982

SECRET

Econ Pol

Public expenditure

21 DEC [illegible]

CONFIDENTIAL

c/c JV

Prime Minister (2)

MES 21/12

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

PRIME MINISTER

MT

LONG TERM PUBLIC EXPENDITURE - EDUCATION

At the meeting you held on 15 December, I quoted some international comparisons in the student loans field in which you and Keith Joseph expressed interest.

..... 2. I now attach the table from which those figures came. It is largely drawn from the Institute of Economic Affairs pamphlet 'Grants or Loans?' published in 1980 (Table 3). The IEA had drawn on OECD and national education department statistics for 1978 (then the latest available), so the material is not up-to-date. The attached table includes references to the newly-announced German and Australian proposals for which we have had to rely on press reports. If Keith Joseph (to whom I am copying this) has any more concrete information on those countries' plans, or can up-date the IEA figures, it would be useful to know.

G.H.

20 December 1982

CONFIDENTIAL

PUBLICLY-FUNDED STUDENT AID OVERSEAS

Country	Proportion of student support			Loan repayments			Students receiving public aid %	Tuition fees payable by student
	means-tested grants	unconditional grants	Loans	Term	Interest+ rate %	Deferral arrangements		
Australia								
present	100%	-	-	-	-	-	38	NO
proposed	•	-	•	•	•	•		
Canada	20%	-	80%	10 years	9	YES	35	YES
France	80%	-	20%	short	0	YES	13	NO
W. Germany								
present	50%	-	50%	20 years	0	YES	40	NO
proposed	-	-	100%	20 years		NO		
Japan	20%	-	80%	20 years	0	YES	10	YES
Netherlands	60%	-	40%	10 years	8	YES	35	YES
Norway	-	20%	80%	20 years	7.5	YES	75	NO
Sweden	-	12%	88%	20 years	3.2	YES	60	NO
USA	60%	-	40%	10 years	8	YES	20	YES

+ 1978 figures.

• A new Australian loans scheme has just been announced to start next year. There is little information available as yet, other than that the present system of means-tested grants will be retained but supplemented by repayable loans.

Source: IEA pamphlet "Grants or Loans?" 1980 (except for Australia and W. Germany proposed schemes, from newpaper reports).

Econ Pol

Public expenditure

21 DEC 1982

SECRET

Econ Pol DSS

10

File

10 DOWNING STREET

From the Private Secretary

20 December 1982

LONG TERM PUBLIC EXPENDITURE: EDUCATION

I am afraid that in my letter to you of 15 December I omitted to mention one of the conclusions of the Prime Minister's meeting on this subject.

It was agreed that there should be an examination of the scope for making savings in teacher costs; and it was recognised that in order to make such savings on a worthwhile scale, it might be necessary to introduce legislation at some stage in the future.

I am sending copies of this letter to John Kerr (HM Treasury), John Gieve (Chief Secretary's Office, HM Treasury), and Richard Hatfield (Cabinet Office). I would be grateful if you and they could ensure that it is seen by only those specifically authorised by your Ministers to do so.

M. C. SCHOLAR

Mrs. Imogen Wilde,
Department of Education and Science.

SECRET

10 DOWNING STREET

From the Private Secretary 20 December 1982

PUBLIC EXPENDITURE WHITE PAPER:
NET PAYMENTS TO EUROPEAN COMMUNITY INSTITUTIONS

The Prime Minister has noted, without comment, your letter of 15 December.

I am copying this letter to Roger Bone (FCO), Robert Lowson (MAFF) and Richard Hatfield (Cabinet Office).

A. J. COLES

Miss Jill Rutter,
HM Treasury.

ECON POL
Sup

c. HO Dtrans
LCO WPO DTde
HMT DI CDL
FCO WO CS-HMT
DES SO DEmp
NIO DEnv. DEng
MOD MAFF WPS
CO DHSS

10 DOWNING STREET

From the Private Secretary 17 December 1982

Dear John,

PUBLIC EXPENDITURE WHITE PAPER

Thank you very much for your letters of 16 December, to which were attached drafts of the 1983 Public Expenditure White Paper.

I showed these to the Prime Minister and she is content, subject to the views of her colleagues, with what is proposed.

I am sending a copy of this letter to the Private Secretaries to all Cabinet Ministers.

Yours sincerely,

Michael Scholar

John Gieve, Esq.,
HM Treasury.

Sup

4.65 CONFIDENTIAL

cc

Prime Minister (2)

I think you have already seen this?

MLS 20/12

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

16 December 1982

Michael Scholar Esq.
10 Downing Street
LONDON
SW1

Dear Michael,

LONG TERM PUBLIC EXPENDITURE: DEFENCE

John Gieve has already sent to you some briefing on long term defence expenditure, as background for the Prime Minister's meeting in January. The Chancellor thought the Prime Minister might also be interested to see the enclosed note which has been prepared within the Treasury. This analyses the 1981 NATO Ministerial Guidance which extended to 1988 the original Alliance agreement to aim at 3 per cent growth. The note also discusses the way in which this aim has been interpreted by other NATO countries.

Yours sincerely,
Margaret O'Mara

MISS M O'MARA
Private Secretary

LTPE: DEFENCE EXPENDITURE

The 1981 NATO Ministerial Guidance extended to 1988 (FY 1988-89) the original 1977 agreement to aim at growth in the region of 3% per annum in real terms (copy attached). The UK subscribed to this guidance.

2. Supporting the principle of the broad 3% aim does not commit any country to achieving it. For example, the UK has for some years endorsed the UN aim that at least 0.7% GDP should be devoted to overseas aid; but the UK has never achieved it.

3. NATO and the individual member countries recognise that implementation of the growth aim has to depend upon countries' economic circumstances. Indeed, the Resource Guidance specifically makes this proviso. Hitherto the UK has accorded defence the utmost priority despite economic difficulties. It seems improbable that UK economic circumstances will permit both indefinite expansion of defence expenditure and reduction in public spending as a whole (central to the economic strategy).

4. That the 3% aim is not binding is demonstrated by countries' achievement and plans to date. Defence expenditure in other European NATO countries has had to take account of harsh economic realities; in some years reductions have been necessitated:

	1980 or 1980-81	1981 or 1981-82	1982 or 1982-83	1983 or 1983-84
US	4.1	7.8	10.3	8.2
UK *	2.8	1.3	3.8	3.3
Germany	2.3	3.3	-0.2	1.4
Italy	4.9	-0.5	2.8	-1.6
Belgium	2.0	0.9	-6.6	-2.3
Netherlands	-1.7	3.3	2.1	1.4

* excludes Falklands expenditure: calculation by MOD's internal pay and price methodology

Source: NATO Defence Planning Committee 1982 General Report

From 1982 onwards, only four other countries in all (US, Canada, Norway, Luxembourg) forecast increases of 3% or more. There are five countries (Belgium, Denmark, Germany, Italy, Netherlands) where defence spending this year and next will either decline in real terms or grow at a rate well below 3%.

5. In terms of money, the UK defence budget is currently second only to the US. On present expenditure plans - which provide for 3% real growth each year with Falklands costs on top - the UK's defence effort in 1985-86 will compare even more favourably with the rest of Europe.

6. There is nothing in the NATO guidance which suggests that only NATO-dedicated expenditure counts against the aim. Nevertheless, on top of "NATO" spending, the UK will also have committed by 1985-86 some £3 billion on "Falklands" expenditure. As Cmnd 8758 (the Falklands White Paper) recognises, much of the "Falklands" spend will benefit the UK defence effort (and thus NATO) as a whole.

7. The rest of NATO will no doubt encourage the UK to continue to increase defence spending indefinitely while tempering their own commitments with economic realism. But the UK would be entitled to rest on its laurels - at least until other Allies catch up with our achievement. Such a position ought to be easy to sustain in Brussels. Indeed, with £3 billion extra "Falklands" provision before 1985-86, the UK could claim to have exceeded its Cmnd 8288 commitments and achieved all its 3% growth well in advance.

NATO CONFIDENTIAL

1977 Resource Guidance

Text of Paragraphs 42 and 43 of DPC/D(77)6(Final)

"42. Accordingly, if a continued deterioration in the NATO-Warsaw Pact balance is to be avoided, an annual increase in real terms (i.e. after full compensation for the inflationary impact of rising pay and price levels) should be aimed at by all member countries. This annual increase should be in the region of 3%, recognizing that for some individual countries:

- economic circumstances will affect what can be achieved;

- present force contributions may justify a higher level of increase.

43. It is moreover indispensable that nations increase the cost-effectiveness of their defence expenditures, i.e. that they improve the share of capital expenditures devoted to major equipment, as well as the amounts of these categories per soldier, but without detriment to combat readiness. Improved methods of assessing cost-effectiveness should be developed."

Defence:

Budget:

1

Prime Minister

Content with this draft (see X overleaf)?

MCS 16/12

Treasury Chambers, Parliament Street, SW1P 3AG

Yes m

Michael Scholar Esq
Private Secretary
10 Downing Street
London SW1

16 December 1982

Dear Michael

held in separate folder

PUBLIC EXPENDITURE WHITE PAPER - PART 1

... I attach two copies of a near-final draft of Part 1 of the 1983 Public Expenditure White Paper. In response to the views of the Treasury and Civil Service Committee, publication is being brought forward from Budget Day to around the end of January. To meet this, final copy has to be with the printer before Christmas.

The figures and text are close to finality, but further minor changes, particularly to correct the figures, will continue to be incorporated until copy is sent to the printer.

The Chief Secretary has asked me to draw attention to some changes from last year.

The basic structure and design of Part 1 will be very similar to last year. But the material on local authority expenditure is considerably shorter. The remaining local authority material has been transferred to a new chapter in Part 2. This reflects, amongst other things, the way local authority current expenditure is actually handled in the Survey.

Because of the prominence given this year to the Autumn Statement, it is necessary to reconcile the White Paper figures with the Autumn Statement. The largest change is the inclusion of a shortfall figure for 1983-84. It is partially offset by increases elsewhere, in particular on social security, and because local authorities are not now to pay NIS at the lower rate until 1984-85.

For the later years, the Chief Secretary has decided to describe the figures which previously appeared in the 'Contingency Reserve' line as a 'Provisional Reserve'. This reflects more accurately their role, which is as a general allowance for future uncertainty. They thus provide for transfers to programmes and for shortfall, as well as for contingencies. The Chief Secretary has reviewed the figures, as he indicated he would in his Cabinet paper, particularly

16 DEC 1982

in the light of the latest information about expected shortfall in 1983-84. He had decided to reduce the provisional reserve in 1984-85 and 1985-86 from £4 billion to £3 billion.

Finally, a cost terms table is now included in Part 1. The Chief Secretary considers that this is inevitable, now that cost terms figures have been given to the TCSC. The table shows a rise in cost terms between 1982-83 and 1983-84. This is due, not to a rise in the 1983-84 plans, but to the greater underspending in 1982-83, which has reduced the estimated outturn in that year. (The comparison of plans with plans shows a fall.) The text therefore makes no comparisons between years, and indeed warns of the danger of doing so. But comparisons will inevitably be made, and this point will need to be covered in briefing at the time of publication. The Chief Secretary proposes to stress in particular the ratios to GDP, which do show a falling trend.

Copies of this letter, with copies of the draft, go to the Private Secretaries of all Cabinet Ministers. A further copy is enclosed with each letter for the Department's PFO.

Yours sincerely

JSl. Gieve

JOHN GIEVE
Private Secretary

Eco Pol

CHIEF SECRETARY TO THE TREASURY

Treasury Chambers, Parliament Street, SW1P 3AG

Michael Scholar Esq
No.10 Downing Street
London SW1

16 December 1982

Dear Michael

PUBLIC EXPENDITURE WHITE PAPER: PARTS 2-5

to PM 16/12/82 one copy (attached to only letter) ... Following my earlier letter circulating Part 1, I now attach two copies of the remainder of the draft White Paper.

The only point I should add to those in my earlier letter relates to output measures. In commenting on last year's White Paper, the Treasury and Civil Service Committee stressed the desirability of including as much output information as possible. The Government in reply accepted this. Progress has been made in a number of areas, but the overall picture is patchy. The Chief Secretary considers that further progress will have to be made next year if the Government is not to face criticism from the TCSC.

Copies of this letter, with copies of the draft, go to the Private Secretaries of all Cabinet Ministers. A further copy is enclosed with each letter for the Department's PFO.

Yours sincerely

JSt. Gieve

JOHN GIEVE
Private Secretary

Main points from the White Paper

The Government's revised expenditure plans for 1983-84 are some £¾ billion lower than the plans in the last White Paper (Cmnd 8494). This is some £½ billion lower than the plans set out in the Autumn Statement on 8 November 1982: it incorporates some adjustments to the programme totals as well as the shortfall implied in the Industry Act Forecast set out in Part 1 of the Autumn Statement. The planning total is now £119½ billion.

For 1984-85 and 1985-86, the provisional planning totals are £126½ billion and £132½ billion.

The main changes in the expenditure plans for 1983-84 compared with Cmnd 8494 are increases for local authority current expenditure (£1.3 billion), social security (£0.8 billion) and defence (£0.6 billion), and a reduction in the contingency reserve (£2.5 billion).

Total public sector capital expenditure in 1983-84 (£11¼ billion) is planned to be 12% higher than the outturn expected for 1982-83. Expenditure on construction is expected to rise by 9% to £11 billion. In 1982-83, there has been substantial capital underspending - mainly by the nationalised industries and local authorities. The Government are taking steps to prevent such underspending in future years.

Planning totals(1) £ billion cash

	1980-81	1981-82	1982-83	1983-84	1984-85	1985-86
January 1979 White Paper (Cmnd 7439)(2)	96.1	110.4	120.0			
March 1980 White Paper (Cmnd 7841)(2)	91.0	101.7	106.3	112.3		
March 1981 White Paper (Cmnd 8175)(3)(4)	92.7	104.7	109.9	113.6		
March 1982 White Paper (Cmnd 8494)(5)	93.1	105.7	114.8	120.3	127.6	
Estimated outturns/ present plans	92.8	104.6	[113.1]	[119.6]	[126.4]	[132.3]

(1) As defined in this White Paper.

(2) Converted into cash using the same inflation assumptions as used for converting the plans in Cmnd 8175. See footnote (3).

(3) Converted into cash as explained in page 103 of Cmnd 8494 Vol 2.

(4) Including changes announced in the Budget Statement on 10 March 1981.

(5) Including changes announced in the Budget Statement on 9 March 1982.

3.1

Public Expenditure White Paper - Part 1

The Expenditure Plans

Introduction

1. This White Paper sets out the Government's plans for expenditure for the years 1983-84 to 1985-86. The plans are summarised in Table 1.1, which shows the composition of the planning total. Chart 1.2 shows the planning total for each year.

2. The planning total for 1983-84 is £[119.6] billion, some £[¾] billion lower than the plans for that year set out in the last White Paper (Cmnd 8494 of March 1982) after taking account of Budget changes, and some £[6½] billion higher than the latest estimated outturn for 1982-83. The planning totals for 1984-85 and 1985-86, £[126.4] billion and £[132.3] billion respectively, are provisional and will be reviewed in the 1983 survey. The 1984-85 total in the last White Paper after taking account of Budget changes was £127.6 billion.

3. In 1982-83 the total outturn, at £[113.1] billion is expected to be some £[1¾] billion below plan. The excess of local authority current expenditure compared with plan is expected to be more than offset by lower expenditure on local authority capital, central government votes, and by the nationalised industries.

Changes since Cmnd 8494

4. Table 1.11 shows the changes since Cmnd 8494. Further detail is in the programme chapters and table [4.7] in Volume 2.

5. The main changes in the expenditure plans compared with Cmnd 8494 are increases in local authority current expenditure (£1.3 billion), social security (£0.8 billion) and defence (£0.6 billion), and a reduction in the contingency reserve (£2.5 billion). Nationalised industries' total net external finance is close to that in Cmnd 8494 (see paragraph 19): but expenditure has been switched within the total to grants from borrowing.

6. The main features of the plans for 1983-84 were published in the Autumn Statement on 8 November 1982. This White Paper incorporates a number of changes which have been made since then: these are set out in Table [4.7] of Volume 2. They reflect revised estimates of expenditure in relation to the European Community, revised estimates of the

pattern and take-up of social security payments,and more refined calculation of the effects of the revised economic assumptions given in the Autumn Statement. The expenditure plans of central government and the nationalised industries have been adjusted downwards to offset the reduction in the national insurance surcharge announced on 8 November, the benefit of which is not intended to accrue to the public sector. In 1983-84 only, local authorities will continue to pay the surcharge at the former rate of 2½ per cent, so no similar adjustment has been made. The provision for local authority expenditure has, however, been adjusted downwards for 1984-85 and 1985-86. The planning totals now also incorporate the reduction for estimated net shortfall which, for 1983-84, was embodied in the Industry Act Forecast set out in Part 1 of the Autumn Statement. The net effect of these changes is to reduce the planning total by some £½ billion.

7. From 1983-84 onwards, funds have been transferred from the Property Services Agency to departmental programmes to provide for the start of the new Property Repayment Service (see Chapter 2.14 in Volume 2), and from the Management and Personnel Office to departmental programmes to provide for the introduction of a system of repayment for the services of the Civil Service College (see Chapter 2.13 in Volume 2). These changes do not affect the planning total.

Main features of programmes

8. Chart 1.2 and table 1.7 show the main programmes as now planned.

Social Security

9. By far the largest single programme is social security. It accounts for over one-quarter of the total, nearly all ~~is~~ on benefits, over half on benefits payable to those over retirement age.

10. For the social security projections, the assumption is that the retail prices index will rise by 5% between November 1982 and November 1983. Illustrative assumptions are made that prices will rise by 5% and 4% respectively in the next two years,and that unemployment (Great Britain, excluding school leavers etc) will average 2.7 million in 1982-83 and 3.0 million a year thereafter.(1) The unemployment assumption is not a forecast or prediction, and the maintenance of the assumption for the later years at the same level as for 1983-84 follows the usual convention. The unemployment levels in the later years may turn out to be lower than has been conventionally assumed if developments in the world

---

(1) These assumptions are on the 'claimants' basis now used by the Department of Employment for the unemployment count. The figures are consistent with those given in the Autumn Statement, which were on the old 'registrations' basis.

economy are favourable and developments at home - notably by way of continued reduction in pay settlements - permit.

11. The increase of some £[800] million in the plans for 1983-84 results mainly from two factors. First, the unemployment assumption (see paragraph 10) is higher than previously. Second, in the light of the latest information, the likely pattern of benefit claims has been reassessed: there are higher estimates of numbers in receipt of retirement pension and invalidity benefit, and of one-parent families, the disabled and long-term sick in receipt of supplementary allowance. These increases would have been larger still, but they have been partly offset by the decision announced in the Autumn Statement that the 1983 uprating will take account of the amount by which the 1982 uprating exceeded what is required to maintain full price protection. The overall increase in the social security programme has been reduced by £180 million in 1983-84, by £530 million in 1984-85 and by £600 million in 1985-86. Final and detailed decisions about the composition of expenditure in 1983-84 will be announced in the context of next year's Statement on the uprating of social security benefits.

Defence

12. The provision meets the Government's commitment to plan to implement the NATO aim of 3% real growth per annum, with Falklands costs in addition. Additions are mainly in respect of defence costs associated with the Falkland Islands: provision for the latter amounts to £624 million in 1983-84, £684 million in 1984-85 and £552 million in 1985-86.

Employment

13. The plans provide for expenditure on two new special employment measures, the Community Programme and Job Splitting Subsidy, announced on 27 July 1982. The gross cost (some £260 million in 1983-84) is included in the employment programme. The related savings on social security benefits are taken into account in the social security programme. Taking the two together, the net increase in public expenditure as a result of these measures is some £100 million in 1983-84, rising to about £200 million the following year and £235 million in 1985-86.

Law and Order

14. The increase of £[96] million in the Home Office plans for 1983-84, and corresponding increases [of £ million in 1984-85 and £ in 1985-86], reflect the Government's continuing emphasis on the fight against crime. The main increase is for the police, but there is also a substantial increase for prisons, with smaller additions for the probation services and magistrates' courts.

Health

15. Compared with previous plans, expenditure on the National Health Service in England is planned to increase by £80 million in 1983-84, £84 million in 1984-85 and £87 million in 1985-86. This is for health authority services, new central initiatives for service improvements, and welfare milk and should allow some further real growth in the hospital and community health services.

Education and Science.

16. The plans allow for an extra £60 million in 1983-84 (and £130 and £50 million in the two following years) as part of the increase in provision for local authority current expenditure (see paragraph 23 below). Extra resources will also be provided for a special programme for the recruitment of young researchers in the universities, partly offset by a reduction in the previously planned value of the student grant.

Analysis by Spending Authority

Central Government

17. Central government expenditure in aggregate accounts for nearly three-quarters of total programmes. Of this:

rather less than half is on goods and services, mainly for defence and the national health service; the pay and related costs of the civil service, amount to just under one-tenth of central government expenditure;

slightly over a third is social security benefits;

the remainder is other transfer payments, such as housing subsidies, industrial support and lending to the nationalised industries.

The figures are summarised in Table 1.3.

Nationalised Industries

18. The nationalised industries' external finance is shown in Table 1.4. Part 3 sets out changes of coverage and shows the External Financing Limits for individual industries in 1983-84. As in previous White Papers, no comparable financing breakdown is shown for subsequent years. The finances of trading bodies such as nationalised industries depend on trading conditions and results, and there may be large swings in either direction for individual industries.

Table 1.4 Nationalised industries' external finance

£ million cash

	1982-83 estimated outturn	1983-84 plans	1984-85 plans	1985-86 plans
Borrowing from Government (net)	1248	1119	1277	1018
Market and overseas borrowing (net)	-866	-200	-352	-546
Grants	1840	1704	1336	1380
Total external finance	2222	2624	2261	1852

19. Total net external finance for the nationalised industries increases by [£54m] in 1983-84 compared with the 1982 White Paper (Cmnd 8494). (Table 1.11 shows increases in total borrowing only; the increases in grants are included in the changes shown for the relevant programmes). Planned investment is slightly higher at £6.8 billion. The Government are encouraging industries to fulfil their investment plans. If 1983-84 plans are fulfilled, investment will increase by 11 per cent over the estimated outturn for 1982-83 (excluding the British National Oil Corporation). The industries as a whole are planning to finance nearly two-thirds of their investment from internally generated funds.

20. Nationalised industries generally expect to have lower internal resources than forecast in Cmnd 8494 as a result of lower demand, lower inflation assumptions and other factors. Tariffs are expected to rise overall by no more than the Retail Price Index in 1983-84. Industries' aggregate needs for external finance are forecast to decline by about 30 per cent between 1983-84 and 1985-86. By far the largest amounts of external finance are for British Rail and the National Coal Board.

21. These plans depend on the industries keeping current costs including wage costs under control in the way that private sector companies have to do. Failure to do this is likely to mean either higher prices or less investment. The Government are continuing to press for greater efficiency both through introducing market disciplines wherever possible and by other mechanisms, such as tight external financing limits and the programme of enquiries by the Monopolies and Mergers Commission and outside consultants.

Local authorities

22. Public expenditure by local authorities is shown in table 1.5. Further information is contained in Chapter 2.18.

23. In 1982-83, local authorities budgeted to spend some £1½ billion more relevant current expenditure than envisaged in Cmnd 8494. This inevitably has an impact on the following year and the previous provision for 1983-84 would therefore now be unrealistic. The government accordingly recognises that local authority expenditure in 1983-84 will be more than desirable. Provision has been raised by £1.3 billion. Most of this increase has not been assigned to services and is in the form of a general addition reflecting the fact that some local authorities will need more time to moderate their expenditure.

Public Expenditure by local authorities in Great Britain — Table 1.5

£m cash

	1981-82 outturn	1982-83 budgets	1983-84 plans	1984-85 plans	1985-86 plans
Current expenditure	22931	25304 (a)	25731	26537	27463
of which not allocated to services	-	-	1024	580	347
Capital expenditure	3264	3556	3922	4242	4479
Total	26195	28860 (b)	30677 (c)	31359 (d)	32289 (d)

(a) Local authorities' budgets. No shortfall allowed for.

(b) Local authorities pay NIS at 3½% in 1982-83.

(c) NIS at 2½% in 1983-84

(d) NIS at 1½% thereafter.

Special sales of assets

24. Net sale proceeds from special sales of assets in 1982-83 are expected to total £550 million, compared with the original target of £660 million. Net proceeds from the sale of Britoil amount to £334 million in 1982-83 with a further £293 million expected in 1983-84. The Government plan to dispose of the British Gas Corporation's major offshore oil interests in 1983-84 and have announced their intention to transfer British Airways and British Telecom to the private sector in due course. The Government intend, after the next election, to offer up to 51 per cent of British Telecom's shares on the market in one or more tranches.

25. Target proceeds from special sales of assets have been set at £750 million in 1983-84 (an increase of £150 million since Cmnd 8494), £1500 million in 1984-85, and £500 million in 1985-86.

26. Because future special sales of assets figures are likely to vary in content, timing and market conditions, no attempt is made to break down present and future year figures. Details for 1981-82 are included in Part 4.

Contingency Reserve for 1983-84

27. The plans for 1983-84 include a reserve for contingencies and policy changes during the course of the year. The Contingency Reserve is a control figure for the year ahead: any fresh decisions to incur expenditure which cannot be accommodated within existing programmes will be contained within it. For 1983-84 it is provisionally set at £1500 million. This is smaller than in either of the previous two years. It was £2500 million in 1981-82 and £2400 million in 1982-83. The amounts provided in these years turned out to have been unnecessarily large.

Provisional Reserves for later years

28. Provisional reserves of £3 billion have been provided in both 1984-85 and 1985-86. This is an overall figure to cover the requirements of the Contingency Reserves for those years (which will be determined in future surveys and will then form a control figure) as well as possible shortfall and further programme requirements.

Debt Interest

29. Table 1.1 shows two figures of debt interest. The net definition of debt interest represents, broadly, interest payments financed from taxation or further Government borrowing. Gross debt interest represents total payments of debt interest by the public sector as defined in the National Accounts: it thereby includes (unlike the net definition) interest payments matched by interest receipts or by provision for interest in the accounts of public trading activities. Table [4.5] of Volume 2 reconciles the two definitions.

Capital and Current expenditure

30. Tables 1.8, 1.9 and 1.10 provide an analysis of total public expenditure by spending authority and economic category. Table 1.13 shows the expected expenditure on construction. The Government have not taken decisions about the allocation of expenditure in the later years in sufficient detail for the analysis to be extended beyond 1983-84.

31. The main changes in current expenditure between 1982-83 and 1983-84 are less for housing subsidies, more for social security benefits ('current grants to persons') and more for defence expenditure ('current expenditure on goods and services') in respect of the Falkland Islands. Compared with previous plans (Cmnd 8494 - see table 1.12), current expenditure is now planned to increase by some £2 billion. The main factors are those indicated above, together with the increased provision for local authority current expenditure.

32. Capital expenditure (which is defined as excluding capital spending by the nationalised industries, but including all of their borrowing) is planned to be about £11¼ billion in 1983-84. Nationalised industries' capital expenditure is shown in Table 3.2 of Volume 2. Total construction expenditure, including investment on construction planned by the nationalised industries, is expected to be some £11 billion, an increase of over 9% compared with the estimated outturn for 1982-83 of some £10 billion. All these figures exclude a substantial element of defence expenditure on capital works and equipment (see notes to table 1.15), which following international conventions is classified as current expenditure on goods and services.

33. Capital expenditure in 1983-84 is expected to be some 12% higher than the estimated outturn for 1982-83 (put at about £10 billion). The Government are concerned about the failure of local authorities and nationalised industries to spend fully the capital provision available to them. The success of the Government's policy on the sale of council houses has generated substantial capital receipts. These receipts are available to local authorities to spend above their basic allocations, but in general they have not spent them. The Prime Minister wrote to local authorities and nationalised industries in November 1982 explaining the Government's concern, and steps are being taken (including changes in the capital allocation procedures for local authorities) to combat underspending in future years.

Public Expenditure and GDP

34. The ratio of public expenditure (including net debt interest and certain other adjustments) to gross domestic product (GDP) was 44½ per cent in 1981-82 (see chart 1.6). Using the expected outturn of expenditure and the Industry Act forecasts of GDP the 1982-83 ratio is expected to be [44 per cent], falling further to [43½ per cent] in 1983-84.

Cash limits

35. The White Paper plans for the year ahead (1983-84) will be translated directly into cash limits, which are the control figures for the coming year. The great majority of limits, are on voted expenditure and are published in the Estimates. Others, mostly covering capital expenditure by local authorities and expenditure by Northern Ireland departments, will be published at the same time. Cash limits will not normally be changed during the year. Any increases in cash limits which are decided will be charged to the Contingency Reserve.

36. 40% of public expenditure is directly cash-limited. This includes the External Financing Limits of the nationalised industries. Another 40% consists of "demand-determined" services where, once policy and rates of payments have been determined, expenditure in the short term depends on the number of qualified applicants: eg social security benefits. The remaining 20% is local authority current expenditure: the rate support grant, the Government's main contribution to the financing of such expenditure, is subject to a cash limit, but not the expenditure itself.

Manpower

37. The Civil Service has been reduced from 732,300 in April 1979 to 655,000 in October 1982, a fall of nearly 11%. A further reduction to 630,000 is planned by the end of 1983-84 - a total reduction of 14%. The Civil Service will then be smaller than at any time since the end of the Second World War. For the armed forces, Cmnd 8288 identified manpower reductions of up to 19,500 by 1986 (6% less than in 1982). The Government are considering any need to adjust this in the light of Falklands commitments.

38. Between 1979 and 1981 total NHS manpower in Great Britain increased by 58,700 (whole-time equivalents) to 998,300, ie about 6½ per cent and broadly in line with the increase in resources to the Service. About 80 per cent of the increase was for manpower directly involved in patient care; nursing and midwifery staff accounted for 70 per cent of the increase. In England the Government set a target of a 10% reduction over the years to 1984-85 in health authorities' management costs as a proportion of their resources. Comparable measures are in hand in Scotland and Wales. The measures which the Government are taking to ensure that health authorities progressively increase efficiency within the resources allocated to them are described in Volume 2, Chapter 2.11. In particular, in England, manpower targets are being set, and there is to be a management enquiry into the NHS's use of manpower.

39. Local authorities' manpower in Great Britain has been reduced by over 81,000 (full-time equivalents), or 3.5%, from 2,347,740 at March 1979 to 2,266,400 at June 1982. Further savings are envisaged in the expenditure plans. The largest fall in manpower has been in the education service which employs nearly half of local government workers: numbers fell by over 70,000, or 6%, between 1979 and 1982. The staff employed on law, order and protective services increased by 12,000 (6%) over this period, consistent with the Government's priorities.

Pay

40. Pay accounts for some 30% 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. For the civil service, armed forces and other central government groups apart from the National Health Service, the present plans are based on the Government's decision, announced on 1 October 1982, to provide in 1983-84 for average increases in wages and salaries bills of 3½ per cent from due settlement dates, after taking account of planned manpower changes.

Public expenditure in 1981-82 and 1982-83

41. The outturn of expenditure in 1981-82 is now put at £104.6 billion about £1 billion less than the estimated outturn published in Cmnd 8494 after adjusting for classification changes since then.

42. When this White Paper went to press, outturn for 1982-83 was estimated centrally at about £113.1 billion, compared with the revised plans of £114.7 billion published in the Autumn Statement. But this is a very tentative estimate. Almost £1 billion of this shortfall represents an estimate of that part of the Contingency Reserve which will not be required, and the rest is split almost equally between central government and the external financing limits of the nationalised industries. In aggregate, local authority expenditure is expected to be as planned; however, this reflects overspending on current expenditure and underspending on capital.

Cost terms

43. The only table not in cash is table [1.14] which expresses the figures in cost terms for years up to and including 1983-84. Any comparison between 1982-83 and 1983-84 is, of course, a comparison between estimated outturn and plan and needs to be treated, therefore, with considerable caution. Cost terms figures are the cash outturn or plans adjusted for the effect of general inflation, as measured by the GDP deflator, to a 1981-82 price base. They are not the same as the volume figures used in public expenditure White Papers before Cmnd 8494. Changes in cost terms figures from year to year show the combined effect of:

i. changes in the quantity of goods and services bought in past years, or notionally provided for in future years, (or, for transfer payments, numbers of beneficiaries and levels of support) and;

ii. changes in their relative prices; that is in the extent to which relevant prices have differed, or may differ, from average price movements as measured by the GDP deflator.

~~PEWP PART 2 TABLES~~

PLANNING TOTAL

Table 1.1 £ million cash

	1977-78	1978-79	1979-80	1980-81	1981-82	1982-83	1983-84	1984-85	1985-86
Public expenditure programmes									
1.Central government (including Government finance for nationalised industries)	39,747	46,839	56,230	67,912	76,943	85,851	88,610		
2.Local authorities	16,301	17,996	21,608	25,117	26,665	29,160	30.180	124,760	130090
3.Certain public corporations capital expenditure	472	457	581	759	687	756	488		
Adjustments									
4.~~Nationalised industries~~ Public corporations' net overseas and market borrowing	817	443	-481	-617	193	-1,085	-292	-440	-660
5.Special sales of assets(net)	-548		-999	-356	92	-550	-750	-1,500	-500
6.Local authority current expenditure not allocated to programmes							1,024	580	350
7.Contingency reserve					~~300~~	~~1,228~~ 200(1)	1,500	3~~4~~,000	3~~4~~,000
7.General allowance for shortfall						-1,200	-1,200		
9.Planning total	56,789	65,735	76,939	92,816	104,~~880~~ 550	~~114,161~~ 113133	119,560	12~~7~~6,390	13~~3~~2,280
10.Percentage change on previous year									
Memorandum items									
a. Debt interest -gross(2) -net(2) (not included above)	1,842	2,384	3,714	4,634	6,200	[6.500]	[7,000]	[7,500]	[7,800]
b. Nationalised industries' total net borrowing (included in lines 1 and 4)	718	1,163	1,537	1,752	1,876	424	912	910	400

i) Amount shown is expected to be fully spent by the end of the year.

2) See paragraph 29.

1982-83 to 1985-86

Chart 1.~~3~~ 2 Public expenditure by programme £ million cash ~~1981-82 to 1984-85~~

Year	£ million	Programme
1982-83	12,634	Defence
1983-84	14,103	
1984-85	15,300	
1985-86	16,440	
1981-82	1,647	Overseas aid and other overseas services
1982-83	2,139	
1983-84	2,330	
1984-85	2,450	
1981-82	1,557	Agriculture, fisheries, food and forestry
1982-83	1,534	
1983-84	1,490	
1984-85	1,500	
1981-82	5,602	Industry, energy, trade, employment
1982-83	5,845	
1983-84	4,860	
1984-85	5,030	
1981-82	3,922	Transport
1982-83	4,160	
1983-84	4,340	
1984-85	4,490	
1981-82	3,320	Housing
1982-83	3,480	
1983-84	2,760	
1984-85	2,860	
1981-82	3,471	Other environmental services
1982-83	3,747	
1983-84	3,870	
1984-85	4,030	
1981-82	3,747	Law, order and protective services
1982-83	4,108	
1983-84	4,450	
1984-85	4,700	
1981-82	12,362	Education, science, arts, libraries
1982-83	12,754	
1983-84	13,110	
1984-85	13,410	
1981-82	12,764	Health and personal social services
1982-83	13,633	
1983-84	14,480	
1984-85	15,250	
1981-82	28,618	Social security
1982-83	32,030	
1983-84	33,500	
1984-85	35,400	
1981-82	14,218	Other programmes including Scotland, Wales, N. Ireland
1982-83	15,034	
1983-84	15,870	
1984-85	16,630	
1981-82	2,018	Nationalised industries' total net borrowing
1982-83	934	
1983-84	1,310	
1984-85	770	
1981-82	250	Other (contingency reserve and special sales of assets)
1982-83	1,650	
1983-84	3,400	
1984-85	5,400	
1981-82	**106,130** (estimated outturn)	Planning total
1982-83	**115,150** (plans)	
1983-84	**121,070** (plans)	
1984-85	**128,370** (plans)	

Note.

Table to be redrawn. Figures to be brought into line with Table 1.7. Arts & libraries to be split from Education & Science.

Table 1.3 Central government expenditure

£ million cash

	1977–78	1978–79	1979–80	1980–81	1981–82	1982–83	1983–84	1984–85	1985–86
~~Central government:~~									
Defence	6,821	7,496	9,227	11,180	12,606	14,411	15,987	17,290	18,330
Overseas services	1,567	1,853	2,080	1,624	1,686	2,202	2,173	2,310	2,460
Agriculture fisheries food and forestry	780	698	831	1,179	1,186	1,568	1,596	1,520	1,590
Trade,industry,energy and employment	2,160	2,956	2,771	3,873	5,092	5,658	5,432	5,290	5,220
Transport	977	996	1,240	1,387	1,703	1,896	1,962	2,060	2,120
Housing	1,420	1,651	1,898	2,078	1,483	1,259	1,208	1,190	1,250
Other environmental services	374	435	524	648	623	770	820	860	880
Law,order and protective services	413	487	604	797	945	1,065	1,258	1,340	1,400
Education and science	1,050	1,152	1,388	1,707	1,815	2,089	2,215	2,290	2,390
arts and libraries	107	125	154	174	195	220	231	240	250
Health and personal social services	5,559	6,315	7,534	9,670	10,889	11,779	12,480	13,140	13,720
Social security	13,658	16,176	19,118	23,069	27,932	31,458	32,264	33,690	35,550
Other public services	908	965	1,153	1,431	1,546	1,659	1,663	1,730	1,820
Common services	766	853	1,009	1,099	1,453	1,652	1,000	1,090	1,200
Scotland	1,400	1,585	1,943	2,392	2,575	2,757	2,893	3,020	3,150
Wales	547	658	822	1,010	1,092	1,148	1,217	1,310	1,360
Northern Ireland	1,445	1,731	1,991	2,374	2,653	2,898	3,099	3,250	3,410
Government lending to nationalised industries	-205	706	1,941	2,222	1,470	1,363	1,113	1,250	940
Total ~~central government~~ excluding adjustments (see table 1.1)	39,747	46,839	56,230	67,912	76,943	85,851	88,610	92,860	97,040

Chart 1.6 Ratios of public expenditure[1] to GDP at market prices

[1] Includes payments of VAT by local authorities and non-trading government capital consumption to make the total comparable with GDP at market prices.

4

~~PEWP PART 2 TABLES~~

Total expenditure by programme

Table 1.~~9~~7 — £ million cash

	1977-78	1978-79	1979-80	1980-81	1981-82	1982-83	1983-84	1984-85	1985-86
Defence	6,821	7,496	9,227	11,180	12,606	14,411	15,987	17,290	18,330
Overseas aid and other overseas services									
Overseas aid	599	723	788	888	960	959	1,056	1,100	1,130
Net payments to EC institutions	542	751	839	221	153	580	380	450	530
Other overseas services	426	378	454	515	573	663	737	770	800
Agriculture, fisheries, food and forestry	866	813	1,007	1,347	1,372	1,784	1,754	1,650	1,730
Industry, energy, trade and employment	2,233	3,036	2,881	4,011	5,256	5,854	5,622	5,490	5,410
Transport	2,270	2,447	2,966	3,456	3,898	4,565	4,302	4,530	4,690
Housing	3,418	3,572	4,514	4,457	3,137	2,769	2,792	2,990	3,110
Other environmental services	1,955	2,257	2,702	3,231	3,244	3,656	3,564	3,680	3,800
Law order and protective services	1,791	2,036	2,579	3,167	3,774	4,284	4,583	4,820	5,040
Education and science	7,039	7,755	8,946	10,901	11,828	12,628	12,560	12,910	13,340
Arts and libraries	299	340	404	477	520	579	563	580	600
Health and personal social services	6,542	7,425	8,899	11,362	12,751	13,879	14,608	15,380	16,070
Social security	13,917	16,437	19,417	23,458	28,510	32,473	34,394	35,940	37,890
Other public services	912	969	1,159	1,439	1,556	1,670	1,675	1,740	1,830
Common services	766	853	1,009	1,099	1,453	1,652	1,000	1,090	1,200
Scotland	3,234	3,683	4,447	5,324	5,772	6,059	6,254	6,470	6,710
Wales	1,279	1,477	1,790	2,129	2,243	2,379	2,528	2,610	2,720
Northern Ireland	1,816	2,137	2,452	2,905	3,218	3,562	3,806	4,020	4,210
Government lending to nationalised industries	-205	706	1,941	2,222	1,470	1,363	1,113	1,250	940
Adjustments									
Public corporations' ~~Nationalised industries'~~ net Overseas and market borrowing	817	443	-481	-617	193	-1,085	-292	-440	-660
Special sales of assets	-548		-999	-356	92	-550	-750	-1,500	-500
Local authority current expenditure not allocated to programmes							1,024	580	350
Contingency reserve					~~300~~	200 ~~1,228~~	1,500	3~~4~~,000	3~~4~~,000
General allowance for shortfall						-1,200	-1,200		
Planning total	56,789	65,735	76,939	92,816	104,~~880~~ 530	~~114,161~~ 113,133	119,560	12~~7~~6,390	13~~3~~2,280

~~PEWP PART 2 TABLES~~

Total public expenditure by economic category

Table 1.~~10~~8 | £ million cash

	1977-78	1978-79	1979-80	1980-81	1981-82	1982-83	1983-84	1984-85	1985-86
Current expenditure									
Wages and salaries	18,741	20,943	24,826	30,839	34,195	36,038	37,186	38,650	40,190
Other current expenditure on goods and services	10,109	11,536	14,042	16,742	19,574	22,998	24,451	26,060	27,510
Subsidies	3,486	3,998	4,935	6,096	5,964	5,919	5,208	4,720	4,670
Current grants to the private sector	15,778	18,548	22,120	27,057	32,845	37,419	39,417	41,240	43,330
Current grants abroad	1,226	1,605	1,740	1,249	1,233	1,713	1,576	1,680	1,790
Total excluding debt interest and other adjustments	49,341	56,629	67,663	81,982	93,811	104,087	107,837	112,350	117,480
Capital expenditure									
Gross domestic fixed capital formation	5,283	5,237	6,011	6,214	5,027	4,948	5,650	6,640	7,130
Increase in value of stockS	62	57	-14	84	-45	360	311	220	240
capital grants	1,655	1,761	1,871	2,221	2,402	2,965	3,041	3,050	3,170
Net lending to private sector	199	-215	341	545	1,403	1,597	723	400	270
Net lending to nationalised industries and some other public corporations (i)	73	1,531	2,784	3,203	1,973	1,858	1,582	1,740	1,440
Net lending and investment abroad	-106	289	-236	-461	-223	-50	134	360	370
Cash expenditure on company securities (net) (2)	15	4		-1	-54	2			
Total excluding adjustments	7,179	8,663	10,756	11,806	10,483	11,680	11,442	12,410	12,610
Adjustments									
Public corporations' ~~Nationalised industries~~ net overseas and market borrowing	817	443	-481	-617	193	-1,085	-292	-440	-660
special sales of assets	-548		-999	-356	92	-550	-750	-1,500	-500
Local authority current expenditure not allocated to programmes							1,024	580	350
contingency reserve					~~300~~	200 ~~1,228~~	1,500	3 ~~4~~,000	3 ~~4~~,000
General allowance for shortfall						-1,200	-1,200		
Planning total	56,789	65,735	76,939	92,816	104,580 ~~104,880~~	113,133 ~~114,161~~	119,560	12~~7~~6,390	13~~3~~2,280

i) The public corporations are those accorded similar treatment to nationalised industries (see Part 5).

2) Excludes sales of British Petroleum shares in 1977-78 & 1979-80 which are included under 'special sales of assets'.

~~DEWP PART 2 TABLES~~

TOTAL PUBLIC EXPENDITURE BY SPENDING AUTHORITY AND PROGRAMME

Table 1.~~17~~9 — £ million cash

	1977-78	1978-79	1979-80	1980-81	1981-82	1982-83	1983-84	1984-85	1985-86
Central government									
Defence	6,821	7,496	9,227	11,180	12,606	14,411	15,987	17,290	18,330
Overseas services	1,567	1,853	2,080	1,624	1,686	2,202	2,173	2,310	2,460
Agriculture fisheries food and forestry	780	698	831	1,179	1,186	1,568	1,596	1,520	1,590
Trade,industry,energy and employment	2,160	2,956	2,771	3,873	5,092	5,658	5,432	5,290	5,220
Transport	977	996	1,240	1,387	1,703	1,896	1,962	2,060	2,120
Housing	1,420	1,651	1,898	2,078	1,483	1,259	1,208	1,190	1,250
Other environmental services	374	435	524	648	623	770	820	860	880
Law,order and protective services	413	487	604	797	945	1,065	1,258	1,340	1,400
Education and science	1,050	1,152	1,388	1,707	1,815	2,089	2,215	2,290	2,390
arts and libraries	107	125	154	174	195	220	231	240	250
Health and personal social services	5,559	6,315	7,534	9,670	10,889	11,779	12,480	13,140	13,720
Social security	13,658	16,176	19,118	23,069	27,932	31,458	32,264	33,690	35,550
Other public services	908	965	1,153	1,431	1,546	1,659	1,663	1,730	1,820
Common services	766	853	1,009	1,099	1,453	1,652	1,000	1,090	1,200
Scotland	1,400	1,585	1,943	2,392	2,575	2,757	2,893	3,020	3,150
Wales	547	658	822	1,010	1,092	1,148	1,217	1,310	1,360
Northern Ireland	1,445	1,731	1,991	2,374	2,653	2,898	3,099	3,250	3,410
Government lending to nationalised industries	-205	706	1,941	2,222	1,470	1,363	1,113	1,250	940
Total central government excluding adjustments	39,747	46,839	56,230	67,912	76,943	85,851	88,610	92,860	97,040
Local authorities									
Agriculture fisheries food and forestry	86	114	175	168	186	215	157	130	140
Trade, industry,energy employment	73	80	110	138	164	197	191	190	200
Transport	1,215	1,378	1,641	1,977	2,117	2,564	2,234	2,360	2,450
Housing	1,870	1,818	2,412	2,012	1,297	1,159	1,480	1,670	1,780
Other environmental services	1,528	1,755	2,116	2,546	2,576	2,875	2,737	2,810	2,920
Law,order and protective services	1,378	1,549	1,975	2,370	2,829	3,220	3,325	3,490	3,640
Education and science	5,990	6,603	7,558	9,194	10,014	10,538	10,345	10,630	10,950
arts and libraries	192	214	250	302	325	359	331	340	350
Health and personal social services	983	1,110	1,365	1,692	1,862	2,100	2,128	2,240	2,350
Social security	258	261	299	390	579	1,016	2,130	2,250	2,340
Other public services Scotland	1,749	2,012	2,403	2,822	3,122	3,194	3,289	3,360	3,470
Wales	722	807	955	1,099	1,125	1,215	1,293	1,280	1,330
Northern Ireland	256	294	349	408	469	508	539	570	590
Total local authorities excluding adjustments	16,301	17,996	21,608	25,117	26,665	29,160	30,180	31,320	32,500
Certain public corporations Capital expenditure(1) (excluding adjustments)	472	457	581	759	687	756	488	580	550
Adjustments									
Public corporations' ~~Nationalised Industries~~ Net overseas and market borrowing	817	443	-481	-617	193	-1,085	-292	-440	-660
Special sales of assets	-548		-999	-356	92	-550	-750	-1,500	-500
Local authority current expenditure not allocated to programmes						200	1,024	580	350
Contingency reserve					~~300~~	~~1,228~~	1,500	3 ~~4~~,000	3 ~~4~~,000
General allowance for SHORTFALL						-1,200	-1,200		
Planning total	56,789	65,735	76,939	92,816	104,~~880~~ 550	~~114,181~~ 113,133	119,560	12~~7~~6,390	13~~3~~2,280

1) Corporations whose capital expenditure is included in public expenditure; mainly the new town development & housing corporations. These corporations do not include the nationalised industries & water authorities. A list is given in Part 5.

9

TOTAL PUBLIC EXPENDITURE BY SPENDING AUTHORITY AND ECONOMIC CATEGORY

Table 1.~~12~~ 10 — £ million cash

	1977-78	1978-79	1979-80	1980-81	1981-82	1982-83	1983-84	1984-85	1985-86
Central government									
Current:									
Goods and services	17,518	19,628	23,649	29,247	33,151	36,726	39,401	41,790	43,930
Subsidies and grants	19,156	22,656	26,960	32,054	37,308	41,811	42,231	43,540	45,590
Capital:									
Goods and services	1,321	1,406	1,571	1,921	2,111	2,685	2,901	3,010	3,190
Grants	1,555	1,610	1,677	1,990	2,097	2,373	2,321	2,380	2,480
Net lending to nationalised Industries and some other public corporations (1)	73	1,531	2,784	3,203	1,973	1,858	1,582	1,740	1,440
Other net lending and capital transactions	125	8	-410	-504	304	398	173	400	420
Total excluding debt Interest and other adjustments	39,747	46,839	56,230	67,912	76,943	85,851	88,610	92,860	97,040
Local authorities									
Current									
Goods and services	11,332	12,851	15,219	18,333	20,618	22,310	22,236	22,920	23,760
Subsidies and grants	1,334	1,494	1,836	2,348	2,735	3,240	3,969	4,100	4,200
Capital									
Goods and services	3,577	3,469	3,982	3,936	2,537	2,263	2,731	3,460	3,780
grants	90	136	171	202	276	562	687	640	650
net lending and other capital transactions	-32	46	401	299	499	785	558	210	110
total excluding debt interest and other adjustments	16,301	17,996	21,608	25,117	26,665	29,160	30,180	31,320	32,500
Certain public corporations (2)									
Capital:									
Goods and services	447	419	444	441	335	361	329	390	400
Grants	10	15	23	29	29	30	32	30	40
Net lending and other capital transactions	15	22	114	289	323	366	127	150	110
Total excluding Adjustments	472	457	581	759	687	756	488	580	550
adjustments									
Public corporations' ~~nationalised industries~~ net overseas and market borrowing	817	443	-481	-617	193	-1,085	-292	-440	-660
special sales of assets	-548		-999	-356	92	-550	-750	-1,500	-500
Local authority current expenditure not allocated to programmes							1,024	580	350
contingency reserve					~~300~~	200 ~~1,228~~	1,500	3~~4~~,000	3 ~~4~~,000
general allowance for shortfall						-1,200	-1,200		
Planning total	56,789	65,735	76,939	92,816	104,~~880~~ 550	113,133 ~~114,161~~	119,560	12~~7~~6,390	13~~7~~2,280

1) See note (1) to table 1.

2) See note (1) to table 1.

SUMMARY OF DIFFERENCES FROM CMND 8494 (1) BY PROGRAMME

Table 1.11

£m ~~in~~ cash ~~terms~~

	1980-81	1981-82	1982-83	1983-84	1984-85
Defence	-	-31	+307	+559	+720
Overseas aid and other overseas services					
Overseas aid	-1	-13	+9	+41	+30
EEC contributions	-67	+108	+80	-200	-150
Other oversea services	+7	-40	+9	+8	-
Agriculture, fisheries, food and forestry	-18	-161	+271	+252	+130
Industry, energy, trade and employment	-176	-337	+27	+692	+400
Transport	-30	-24	+409	-53	+20
Housing	+4	+71	-401	+33	+120
Other environmental services	-11	-34	+78	-146	-190
Law, order and protective services	-8	+33	+185	+58	+50
To be disaggregated (Education and science, arts and libraries	+8	-8	+450	-	+70
Health and personal social services	-5	-13	+247	+91	+90
Social security	+19	-107	+444	+774	+420
Other public services	-3	-40	-18	-20	-50
Common services	-6	-148	+27	+13	-
Scotland	+30	+49	-8	-32	-40
Wales	-4	-54	-32	+49	+20
Northern Ireland	-	-58	+19	+3	-
Government lending to nationalised industries	-56	-356	+232	-141	+110
Adjustments					
~~Nationalised industries~~ Public corporations' net overseas and market borrowing	-22	+154	-826	-265	+20
Special sales of assets	-	+142	+50	-150	-900
Contingency reserve	-	-300	-2,014	-1,476	-2,420
General allowance for shortfall	-	-	-1,200	-1,200	-
	-	-			-
Planning total	-339	-1866	-1687 (3)	-1,111 (3)	-1540 (3)
Debt interest - gross					
Debt interest - net	-	-	-	-	-
Nationalised industries total net borrowing	-78	-202	-595	-406	+120

1) The Government's Expenditure Plans 1982-83 to 1984-85, March 1982

2) The contingency reserve for 1982-83 in Cmnd 8494 was £2250 million, but it was increased in the March 1982 Budget to £2400 million. Of that, [£1172] million has been allocated & is therefore absorbed in the estimated outturn for the programmes concerned. Another £200 million (shown in line 6 of Table 1.1) is expected to be allocated similarly by the end of the year. The remaining [£1028] million is expected not to be spent.

3) Including changes announced in the Budget Statement on 9 March 1982.

SUMMARY OF DIFFERENCES FROM CMND 8494 IN EXPENDITURE
PROGRAMMES BY ECONOMIC CATEGORY

Table 1.12 £m ~~in~~ cash ~~terms~~

	1980-81	1981-82	1982-83	1983-84	1984-85
Current:					
Goods and services	-167	-22	+1,576	+794	+852
Subsidies and grants	-89	-134	+631	+1,306	+775
Capital					
Goods and services	+6	-279	-328	-128	+273
Grants	+20	+70	+588	+513	+433
Government lending to nationalised industries	-56	-356	+232	-141	+106
Net lending to some other public corporations	-13	-77	-44	-87	-62
Other net lending and capital transactions	-19	-310	-321	-276	-612
Adjustments					
Nationalised industries net overseas and market borrowing	-22	+154	-826	-265	+18
Special sales of assets	-	+142	+50	-150	-900
Contingency reserve	-	-300	-2,044	-1,476	-1,420
General allowance for shortfall	-	-	-1,200	-1,200	-
Planning total	~~-340~~ -339	~~-812~~ -1166	~~-660~~ -1687	-1,111	-538

0

Table 1.143 Capital Expenditure on Construction Work

£ million cash

	1977-78 Outturn	1978-79 Outturn	1979-80 Outturn	1980-81 Outturn	1981-82 Outturn	1982-83 Estimated Outturn	1983-84 Plans
Direct Public Expenditure on New Construction							
Housing - New Dwellings and Improvements	2,217	2,143	2,460	2,357	2,009	1,974	2,274
Other Environmental Services	453	584	735	903	818	802	934
Transport	828	878	1,083	1,229	1,281	1,634	1,586
Education	411	373	421	528	445	382	379
Health and Personal Social Services	358	398	483	629	776	803	857
Other (1)	1,276	1,313	1,628	1,755	1,808	1,491	2,048
TOTAL DIRECT PUBLIC EXPENDITURE ON NEW CONSTRUCTURE	5,543	5,691	6,810	7,401	7,137	7,586	8,078
Grants and Loans to Housing Associations and Improvement Grants	770	858	1,117	863	802	1,267	1,561
EXPENDITURE ON ~~TOTAL~~ NEW CONSTRUCTION EXPENDITURE IDENTIFIED WITHIN THE PLANNING TOTAL (2)	6,313	6,549	7,927	8,264	7,939	8,853	9,639
Nationalised Industries:							
Electricity	159	186	227	284	316	351	370
Gas	144	162	202	304	263	250	285
Railways	131	200	146	155	143	114	132
Coal	97	165	219	321	345	332	329
Other	220	226	164	201	235	253	341
EXPENDITURE ON CONSTRUCTION BY TOTAL NATIONALISED INDUSTRIES (3)	751	939	958	1,265	1,302	1,300	1,457

			1977-78 OUTTURN	1978-79 OUTTURN	1979-80 OUTTURN	1980-81 OUTTURN	1981-82 OUTTURN	1982-83 ESTIMATED OUTTURN	1983-84 PLANS			
GRAND TOTAL			7064	7488	8885	9529	9241	10,153	11096			

Defence;
(1) [Agriculture; Industry, Energy, Trade and Employment; Law, Order and Protective Services; Offices and Accommodation
Some expenditure on new construction for military purposes is classified as current expenditure.

(2) See Table 4.[X] for details of all capital expenditure within the planning total

(3) Certain capital expenditure by the British National Oil Corporation which is classified in the accounts as new buildings and works has been excluded from this table since little of the work is performed by the construction industry

Table 1.1~~3~~4 shows all capital expenditure by the public sector or new construction. /As decisions have not yet been taken in all cases on allocations within the main programmes, it is not possible to extend this analysis into the later years._7

The figures cover capital construction only and do not include repair and maintenance, which now accounts for about 40 per cent of public sector expenditure on work by the construction industry. Also excluded is some defence expenditure on construction (amounting to £X million ~~construction~~) which is also classified as current expenditure. The figures consequently understate the implications of public expenditure for the construction industry, but they also include small amounts of expenditure which is not on work done by the construction industry, for example, on the acquisition of land and existing buildings.

The figures cover the following types of expenditure:

direct spending on new construction;

capital grants and loans to housing associations and improvement grants: these go to finance construction work, except that the figures for housing associations also include finance for their expenditure on the acquisition of land and existing dwellings;

the estimated amount of new construction in the nationalised industries' investment programme.

The first two items are included in the planning total, the last is financed by nationalised industries' internal as well as external resources and thus not included as such in the planning total.

Table 1.14

Public ~~Total~~ expenditure in cost terms(1) ~~by programme~~ by Programme.

£million base year 1981-82

	1977-78	1978-79	1979-80	1980-81	1981-82	1982-83.	1983-84
Defence	11,553	11,486	12,077	12,380	12,606	13,406	14,163
Overseas aid and other overseas services							
Overseas aid	1015	1,108	1,031	983	960	892	936
Net payments to EC institutions	418	1,151	1,098	245	153	540	337
Other overseas services	722	579	594	570	573	617	653
Agriculture, fisheries, food and forestry	1,467	1,246	1,318	1492	1,372	1,660	1,554
Industry, energy, trade and employment	3,782	4,652	3,771	4,441	5,256	5,446	4,981
Transport	3,845	3750	3,882	3,827	3,898	4,247	3,811
Housing	5,789	5473	5,908	4,935	3,137	2,576	2,474
Other environmental services	3,311	3,458	3,537	3,578	3,244	3,401	3,157
Law order and protective services	3,034	3,120	3,376	3,507	3,774	3,985	4,060
Education and science arts and libraries	11,922	11,883	11,709	12,071	11,828	11,747	11,127
	506	521	529	528	520	539	499
Health and personal social services	11,081	11,378	11,648	12,581	12,751	12,911	12,942
Social security	23,572	25,187	25,415	25,975	28,510	30,207	30,471
Other public services	1545	1,485	1,517	1,543	1,556	1,553	1,484
Common services	1,297	1,307	1,321	1,217	1,453	1,537	886
Scotland	5,478	5,644	5,821	5,895	5,772	5,636	5,541
Wales	2,166	2,263	2,343	2,357	2,243	2,213	2,240
Northern Ireland	3,076	3,275	3,209	3,217	3,218	3,313	3,372
Government lending to Nationalised industries	-347	1,082	2,541	2,460	1,470	1,268	986
Adjustments							
Public Corporations' net Overseas and market borrowing	1,384	674	-630	-683	193	-1,009	-259
Special sales of assets	-928	—	-1,308	-394	92	-512	-664
Local authority current expenditure not allocated to programmes	—	—	—	—	—	—	907
Contingency reserve	—	—	—	—	—	186	1,329
General allowance for shortfall	—	—	—	—	—	-1,116	1,063
Planning total(2)	96,187	100,728	100,705	102,775	104,580	105,240	105,922

(1) Cash figures as in table 1.7 adjusted for general inflation as measured by the GDP deflator at market prices. The GDP deflator is assumed to increase by some 7½ per cent in 1982-83 and some 5 per cent in 1983-84 as ~~shown~~ stated in the Autumn Statement 1982, Paragraph 1.36. Rounding as in table 1.7.

(2) Totals do not always add because of rounding.

(2)

Prime Minister

A.J.C. 16/12

cc. Mr. Ricketts
Mr. Ingham

CONFIDENTIAL

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

15 December 1982

John Coles, Esq.,
No.10 Downing Street

Dear John,

PUBLIC EXPENDITURE WHITE PAPER : NET PAYMENTS TO EUROPEAN COMMUNITY INSTITUTIONS

The Chancellor has suggested that his colleagues might appreciate a short commentary on the figures for our net payments to EC institutions included in the draft of the Public Expenditure White Paper which is about to be circulated. For convenience, the relevant section of the draft White Paper is attached. The figures are summarised in the accompanying table.

£ million

	1981-82	1982-83	1983-84	1984-85	1985-86
Cmnd 8494	47	500	580	600	
Survey report		635	430	514	687
Latest estimate	153	580	380	450	530
Change since Cmnd 8494	+106	+80	-200	-150	
Change since survey report		-55	-50	-64	-157

As in other recent years, the projections depend crucially on the assumptions made about future budget refunds. We have assumed that the 1982 agreement will be implemented as intended by the Council, present problems in the European Parliament notwithstanding. The Financial Secretary has minuted separately about these problems. The figures for subsequent years assume that we shall be reimbursed 66 per cent of our net contribution before refunds, as was envisaged in the 30 May 1980 agreement, with no restitution of the alleged 'over-payments' for 1980 and 1981. These refunds are assumed to be paid at the end of the calendar year to which they relate, as under the 26 October 1982 agreement.

/The text

The text makes quite clear, as last year, that the 66 per cent is a 'stylised assumption', based on the May 1980 formula, and not a forecast or a negotiating objective. It does not explicitly say that we have assumed no further restitution of the 'overpayments'. But reference is made to the paragraph of the 1982 agreement relating to 'over-payments', and the assumption of no further restitution is implicit in the description of the 66 per cent refund assumption.

Other important assumptions, both mentioned in the text, are that the 1 per cent VAT ceiling wil be maintained and that our share of CAP receipts, which has risen over the past three years from 5-6 per cent to a little over 10 per cent, will remain at the higher level.

The most striking feature of the new projections is the relatively high figure for the current financial year, followed by the relatively low figure for 1983-84 (see line 3 of table). This reflects the patterns of refunds and VAT payments. We are receiving a lower rate of refund for 1982 than assumed for the later years, and a significant part of it is projected to be paid to us in 1983-84 under the risk-sharing arrangements. As regards VAT, the interaction between movements in the sterling/ecu exchange rate and the Community's rules for calculating VAT liabilities has resulted in a heavy concentration of payments on 1982-83.

The changes compared with the previous White Paper shown in line 4 have resulted from a number of factors. The increase in the 1982-83 figure mainly reflects the lower level of refunds for the current year mentioned already. The reduction in the figures for the two subsequent years reflects partly the spillover of 1982 refunds into 1983-84 and more particularly the higher share of CAP receipts now assumed.

In contrast with previous White Papers, the new White Paper will include projections for receipts from the Community's individual funds, in particular the FEOGA, Regional Development and Social Funds. The text explains that the Government's plans for the areas of expenditure concerned have been influenced by the expectation of receipts from the Community. It is hoped that this change, which was agreed by OD(E) in the summer, will help to allay the anxieties of the Commission, the European Parliament and others who feel that the Community's grants have no effect whatever on domestic public expenditure programmes.

I am copying this letter to Roger Bone (FCO), Robert Lowson (MAFF), and Richard Hatfield (Cabinet Office).

Yours sincerely,

Jill Rutter

JILL RUTTER

Econ Pol
WR

LM
15/12

STATEMENT
WEDNESDAY 15 DECEMBER 1982

HOUSE OF COMMONS

PUBLIC EXPENDITURE: SCOTLAND, 1983-84
STATEMENT BY THE SECRETARY OF STATE FOR SCOTLAND (MR GEORGE YOUNGER)

WITH PERMISSION, MR SPEAKER, I SHOULD LIKE TO MAKE A STATEMENT ABOUT PUBLIC EXPENDITURE ON THE SCOTLAND PROGRAMME IN 1983-84. THE TOTAL FOR THE SCOTTISH PROGRAMME, EXCLUDING AGRICULTURE, WAS ANNOUNCED IN THE CHANCELLOR'S AUTUMN STATEMENT.

I HAVE NOW MADE MY ALLOCATIONS TO PROGRAMMES AND I HAVE COMPLETED MY CONSULTATIONS WITH THE CONVENTION OF SCOTTISH LOCAL AUTHORITIES ABOUT THE RATE SUPPORT GRANT AND HOUSING SUPPORT GRANT SETTLEMENTS. THE DEBATES ON THOSE ORDERS WILL GIVE HONOURABLE MEMBERS A FULL OPPORTUNITY TO DISCUSS THE SETTLEMENTS AND I DO NOT WANT TO ELABORATE ON THEM NOW. THE RATE SUPPORT GRANT ORDER AND REPORT ARE BEING LAID BEFORE THE HOUSE TODAY. IT PROVIDES FOR A TOTAL RELEVANT EXPENDITURE FIGURE OF £3,118M AND AGGREGATE GRANTS OF £1,924.25M. PROVISION FOR CURRENT EXPENDITURE WITHIN THE TOTAL IS £2,660M, £25M MORE THAN THE PROVISIONAL FIGURE WHICH I ANNOUNCED ON 28 JULY. I SHALL SAY MORE ABOUT HOUSING IN A MOMENT.

MY TOTAL PROGRAMME FOR 1983-84 NOW STANDS AT £6,380M; £127M HIGHER THAN THE PLAN FOR 1983-84 SET OUT IN CMND. 8494 AND £309M MORE THAN THE RESOURCES AVAILABLE FOR THE CURRENT YEAR. THE FIGURES ARE ESSENTIALLY ON THE SAME BASIS AS THE AUTUMN STATEMENT. I SHALL CIRCULATE DETAILS IN THE OFFICIAL REPORT.

MY PROGRAMME IS IN TWO PARTS. THERE IS A BLOCK OF PROGRAMMES WITHIN WHICH I HAVE DISCRETION TO ALLOCATE RESOURCES, THE TOTAL OF WHICH IS ADJUSTED BY REFERENCE TO CHANGES IN ENGLISH OR ENGLISH AND WELSH PROGRAMMES; AND THERE ARE TWO PROGRAMMES -AGRICULTURE AND INDUSTRY - WHICH STAND ENTIRELY OUTSIDE THE BLOCK.

THE PROVISION FOR THE PROGRAMMES OUTSIDE THE BLOCK IS VIRTUALLY UNCHANGED FROM THAT ANNOUNCED LAST YEAR EXCEPT FOR A REDUCTION OF £10M IN THE PROVISION FOR THE LAND CLEARANCE AND BUILDING PROGRAMME OF THE SDA. THERE IS EVERY INDICATION THAT THE AGENCY WILL BE ABLE TO ATTRACT PRIVATE CAPITAL TO SUSTAIN THIS ELEMENT OF THEIR PROGRAMME.

IN ALLOCATING RESOURCES TO THE OTHER PROGRAMMES I HAVE KEPT PARTICULARLY IN MIND THREE PRIORITIES; OUR CONTINUING COMMITMENT TO LAW AND ORDER AND THE FIGHT AGAINST CRIME; MAINTAINING GROWTH IN THE HOSPITAL AND COMMUNITY HEALTH AND FAMILY PRACTITIONER SERVICES; AND THE NEED TO STIMULATE CAPITAL INVESTMENT WHEREVER POSSIBLE. OTHERWISE THE PROVISION I HAVE MADE GENERALLY ALLOWS FOR THE CONTINUATION OF EXISTING POLICIES.

ACCORDINGLY THE PROVISION MADE FOR LAW, ORDER AND PROTECTIVE SERVICES IS £446M, ABOUT 10 PER CENT MORE THAN THE AMOUNT PROVIDED IN THE CURRENT YEAR. THE INCREASE PROVIDES FOR THE POLICE SERVICE TO BE MANNED FULLY UP TO AUTHORISED ESTABLISHMENT LEVELS, AND IT ALLOWS FOR AN INCREASE IN THE MANPOWER COSTS OF THE PRISON SERVICE AND FOR GROWTH IN DEMAND FOR LEGAL AID.

THE PROVISION FOR HEALTH AND SOCIAL WORK IS £2,051M, AN INCREASE OF 6.9% OVER THE PLANNED PROVISION FOR THE CURRENT YEAR. FOR THE HEALTH PROGRAMME ALONE THE INCREASE IS £108M. OF THIS, ABOUT £80M IS FOR RECURRENT EXPENDITURE ON HOSPITAL, COMMUNITY HEALTH, WELFARE MILK AND CENTRALLY MANAGED HEALTH SERVICES. THIS SHOULD BE SUFFICIENT TO ALLOW FOR IMPROVEMENT IN THESE SERVICES TO MEET NEW DEMANDS, AFTER PAY AND PRICE INCREASES HAVE BEEN MET, AND TO PERMIT A FURTHER REDISTRIBUTION OF RESOURCES TO HEALTH BOARDS IN ACCORDANCE WITH THE SHARE ARRANGEMENTS. PROVISION FOR SOCIAL WORK IS £314M, AN INCREASE OF £25M - WHICH IS 8.6% OVER PROVISION IN THE CURRENT YEAR. THIS RECOGNISES THE GROWING DEMAND FOR SERVICES FOR THE ELDERLY AND OTHER VULNERABLE GROUPS.

THE PROVISION OF £524M FOR TRANSPORT WILL ENSURE, AMONG OTHER THINGS, CONTINUED WORK ON MAJOR ROADS SUCH AS THE A1, A9, A74, A75 AND A94.

In Education, after allowance is made for the continuing decline in school rolls and the reduction in the National Insurance surcharge, the provision I have made should allow for the maintenance of planned staffing standards, provided pay settlements in 1983 are at a reasonable level. On the same basis, there should be room for modest expansion in further education places. I have also made provision for more places in the Central Institutions for advanced studies in the new technologies.

For Housing, the provision is £656m. I have again sought to reduce the general support to local authority housing revenue accounts through Housing Support Grant so as to make available the largest possible resources for capital expenditure, and I am continuing the Housing Expenditure Limits system with a view to reducing the burden of housing support falling on ratepayers to about £9m below this year's level. Most authorities will be able to maintain their full capital programme while increasing rents by less than £1 per week: only those who have consistently failed to respond to Government policies in this field will require larger increases. As a result I am glad to say that I have been able to provide, after account is taken of expected receipts for the local authorities, the Housing Corporation and the Scottish Special Housing Association to have capital programmes at or above this year's level. Total gross capital expenditure will be about £540m.

On capital expenditure generally, about £420m will be available for local authority capital programmes apart from Housing, also after taking account of expected receipts. This is about £15m more than the comparable planned figure for the current year. About a further £380m will be available for the central government capital programmes, including health, Trunk Roads and investment by the SDA and the HIDB. All in all, this amounts to a gross capital programme of about £1,340m, the bulk of which will be spent on construction projects.

A feature of capital expenditure is the tendency for provision to be underspent. I have already taken measures to minimise underspending this year: I have removed all limits from spending by housing authorities this year on improvement and repairs grants

AND SUPPLEMENTARY CONSENTS OF £17M WERE GIVEN TO LOCAL AUTHORITIES IN RESPECT OF OTHER SERVICES. I HOPE THAT THESE MEASURES WILL ENSURE AN OUT-TURN FOR 1982-83 THAT WILL BE WELL UP TO THE PLAN AND WE SHALL SIMILARLY BE MAKING EVERY EFFORT IN 1983-84 TO SEE THAT THE PROVISION THAT WE HAVE MADE FOR CAPITAL PROGRAMMES IS FULLY UTILISED.

SCOTTISH OFFICE

	1982-83 White Paper (Cmnd 8494) with Budget changes (1)	1983-84 White Paper (Cmnd 8494) with Budget changes (1)	1983-84 Revised (2)
Agriculture, fisheries, food and forestry (3)	155	167	166
Industry, energy, trade and employment	165	169	159
Tourism	8	8	8
Transport	499	528	524
Housing	741	650	656
Other environmental services	626	644	636
Law, order and protective services	403	435	446 (4)
Education and science, arts and libraries	1475	1518	1514
Health and social work	1919 (5)	2050	2051
Other public services	79	83	99 (6)
Common services	1	1	1
Local authority current expenditure not allocated	-	-	120
	6071	6253	6380

Notes

(1) Including other minor changes of classification and allocation. Contributions to the External Financing Limit of the nationalised industries and adjustments for the NI surcharge shown separately in the Autumn Statement have been allocated to programmes.

(2) Some figures may be subject to detailed technical amendment before publication of the 1983 Public Expenditure White Paper.

(3) Treated on GB basis in Autumn Statement.

(4) Includes £6m transferred from PSA (other columns not adjusted).

(5) Includes additional provision for NHS pay settlements announced on 1 July and 16 Novemb

(6) Includes £16m transferred from PSA (other columns not adjusted).

(7) Owing to rounding individual figures may not sum to the totals.

SUBJECT cc MASTER OPS

SECRET file 9 da

cc HMT CSO CO bc JV

10 DOWNING STREET

From the Private Secretary 15 December 1982

Dear David,

Long-Term Public Expenditure: Social Security and Health

The Prime Minister had a meeting yesterday morning, to consider the long-term public expenditure prospect on social security and health. Your Secretary of State, the Chancellor the the Exchequer, the Chief Secretary and Sir Robert Armstrong were also present.

The Chief Secretary said that at the Cabinet discussion on 9 September there had been agreement that the long-term prospect for public expenditure presented a formidable problem to the Government. On social security, Treasury Ministers had examined the case for adopting a different formula for indexing social security benefits from that which currently applied. They had concluded that any new formula would either be difficult to substantiate, or would not necessarily involve savings. The best course would be to return to a discretionary system, in which the scale of an uprating would be determined by the Government unfettered by any statutory formula, but taking account of prices, earnings, affordability and so on.

In discussion, it was argued that, as inflation reduced, so did this problem of indexation also diminish. It was essential to get over to the electorate the message that large upratings of benefits imposed a heavy burden on the working population. Over the past twenty years this burden had shown itself in excessively low tax thresholds, penalising the low-paid. There was much disadvantage in the present system of uprating, in its reliance upon a forecast of inflation which was made well before the period in question. There would be merit in a system which, using modern office technology and administrative techniques, shortened the minimum time necessary between the uprating decision and its implementation; and your Secretary of State should consider a change to using an inflation outturn rather than an inflation forecast, perhaps using the June-to-June RPI figure, which would be available in mid-July each year.

Summing up this part of the discussion the Prime Minister said that the aim should be to maintain the maximum freedom of action in the run-up to the General Election. When pressed to give a pledge

/to link

SECRET

to link social security benefits to either prices or earnings indefinitely, Ministers should say that no responsible Government could give an absolute pledge that index-linking would be maintained come what may. This could also remain the position in the new Parliament, given that the Government's economic strategy should lead to a continuing decline in inflation. Your Secretary of State should discuss with the Chief Secretary how best to achieve these objectives, and to get across the message that high upratings meant a larger burden on the working population. He should also consider the change in the method of uprating which had been discussed.

On health, after a short discussion the Prime Minister said that work on the long-term public expenditure prospect should proceed on the basis that the fundamental structure of the National Health Service should remain intact, as she had said in her speech to the Party Conference in the autumn. But ways must be found of supplementing resources, by raising more income from charges, privatising some parts of the National Health Service, particularly the general, ophthalmic, dental and pharmaceutical services, reducing demand for treatment by charging patients (except, perhaps, in hospital) the full cost of services received and reimbursing them subsequently, and giving further encouragement to the private health sector through fiscal concessions. There would also need to be improvements in management, and greater help from voluntary sources.

I am sending copies of this letter to John Kerr and John Gieve (HM Treasury) and Richard Hatfield (Cabinet Office). I would be grateful if you and they would ensure that it is seen only by those specifically authorised by your Ministers to do so.

Yours sincerely,

Michael Scholar

David Clark, Esq.,
Department of Health and Social Security.

SUBJECT

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bc JV
PG

10 DOWNING STREET

From the Private Secretary

15 December 1982

Dear Imogen,

Long-term Public Expenditure : Education

The Prime Minister held a meeting this afternoon on the long-term public expenditure prospect for education. Your Secretary of State, the Chancellor of the Exchequer, the Chief Secretary and Sir Robert Armstrong were present.

Summing up a short discussion, the Prime Minister said that the Government should not be deterred from introducing a student loan scheme, which might save £400-500 million in 10-12 years time, just because there would be additional expenditure in the first few years as a result, of, say, £20-40 million a year. Your Secretary of State would be working on a scheme on these lines. Any proposal for introducing charges for schooling should not be further pursued. It was recognised that proposals which might be brought forward for different methods of financing universities were unlikely to yield public expenditure savings, although it was possible that a number of institutions would be closed, with consequential savings, as students exercised their greater freedom of choice, and numbers dwindled at the poorer quality institutions. A number of other initiatives were under way, including redesigning the distribution of powers between central and local government on education, and improving the management of the education sector. It was recognised that none of these would yield major savings, although every effort should be made to build into the system what was conspicuously lacking at present - a bias towards economy.

I am sending copies of this letter to John Kerr (HM Treasury), John Gieve (Chief Secretary's Office) and Richard Hatfield (Cabinet Office). I would be grateful if you and they would ensure that it is seen by only those specifically authorised by your Ministers to do so.

Yours sincerely,

Michael Scholar

Mrs. Imogen Wilde,
Department of Education and Science.

SECRET

PA

PRIME MINISTER

LONG-TERM PUBLIC EXPENDITURE: EDUCATION

Here is another Treasury brief prepared for the long-term public expenditure exercise, this time on education. The Chief Secretary knows you have a copy, but Sir Keith Joseph does not - and will presumably have a brief of his own prepared by the DES.

Again you will recall that, under scenario B, public expenditure would rise to 47 per cent of GDP if no action were taken to contain it.

MCS

14 December 1982

Econ Pol
Public Expend

cc Press Office.

SECRETARY OF STATE FOR SCOTLAND

SCOTTISH OFFICE
WHITEHALL, LONDON SW1A 2AU

①

MCS 13/12

1 Mr Scholar

2 Prime Minister

Content?

Yes [illegible]

WR 13/12

Willie Rickett Esq
Private Secretary
10 Downing Street
LONDON SW1

13 December 1982

Dear Willie,

PUBLIC EXPENDITURE: ORAL STATEMENT

We have agreed with the Lord President that it would be possible for my Secretary of State to make an oral statement on public expenditure in Scotland in 1983-84 on Wednesday 15 December. I attach the text of the proposed statement, which has been seen in draft by Treasury officials. Mr Younger would be grateful to have the Prime Minister's approval to make this statement and any comments on the text by close of play on Tuesday 14 December.

I am sending copies of this letter and attachment to the Private Secretaries to members of the Cabinet and to the Offices of the Chief Whip and Sir Robert Armstrong.

Yrs,

Muir.

A MUIR RUSSELL
Private Secretary

DRAFT PUBLIC EXPENDITURE STATEMENT

With permission, Mr Speaker, I should like to make a statement about public expenditure on the Scotland programme in 1983-84.

I have now made my allocations to programmes within the Scottish block and I have completed my consultations with COSLA about the Rate Support Grant and Housing Support Grant settlements. The debates on those Orders will give hon Members a full opportunity to discuss the settlements and I do not want to elaborate on them now. The Rate Support Grant Order and report are being laid before the house /¯today_7 . It provides for a total relevant expenditure figure of £3,113.5m and aggregate grants of £1,924.25m. Provision for current expenditure within the total is £2,656m, £21m more than the provisional figure which I announced on 28 July. I shall say more about housing in a moment.

My total programme for 1983-84 now stands at £6380m; £127m higher than the plan for 1983-84 set out in Cmnd 8494 and £309m more than the resources available for the current year. The figures are essentially on the same basis as the Autumn Statement. I shall circulate details in the Official Report.

My programme is in two parts. There is a block of programmes within which I have discretion to allocate resources, the total of which is adjusted by reference to changes in English or English and Welsh programmes; and there are two programmes - Agriculture and Industry - which stand entirely outside the block.

The provision for the programmes outside the block is virtually unchanged from that announced last year except for a reduction of £10m in the provision for the land clearance and building programme of the SDA. There is every indication that the Agency will be able to attract private capital to sustain this element of their programme. I stress that the industrial support programme of the Agency is not being cut.

In allocating resources to the other programmes I have kept particularly in mind three priorities; our continuing commitment to law and order and the fight against crime; maintaining growth in the Hospital and Community Health and Family Practitioner Services; and the need to stimulate capital investment wherever possible. Otherwise the provision I have made generally allows for the continuation of existing policies.

Accordingly the provision made for Law, Order and Protective Services is £446m, about 10 per cent more than the amount provided in the current year. The increase provides for the police service to be manned fully up to authorised establishment levels, and it allows for an increase in the manpower costs of the prison service and for growth in demand for legal aid.

The provision for Health and Social Work is £2051m, an increase of 6.9% over the planned provisions for the current year. For the Health programme alone the increase is £108m. Of this about £80m is for recurrent expenditure on hospital, community health, welfare milk and centrally managed health services. This should be sufficient to allow for improvement in these services to meet new demands, after pay and price increases have been met, and to permit a further redistribution of resources to Health Boards in accordance with the SHARE arrangement. Provision for Social Work is £314 million, an increase of £25m - which is 8.6% - over provision in the current year. This recognises the growing demand for services for the elderly and other vulnerable groups.

The provision of £524m for Transport will ensure, among other things, continued work on major roads such as the A1, A9, A74, A75 and A94.

In Education, after allowance is made for the continuing decline in school rolls and the reduction in the National Insurance surcharge, the provision I have made should allow for the maintenance of planned staffing standards, provided pay settlements in 1983 are at a reasonable level. On the same basis, there should be room for modest expansion in further education places. I have also made provision for more places in the Central Institutions for advanced studies in the new technologies.

For Housing, the provision is £656m. I have again sought to reduce the general support to local authority housing revenue accounts through Housing Support Grant so as to make available the largest possible resources for capital expenditure, and I am continuing the Housing Expenditure Limits system with a view to reducing the burden of housing support falling on ratepapers to about £9m below this year's level. Rent authorities will be able to maintain their full capital programme while increasing rents by less than £1 per week: only those which have consistently pursued low rent policies will require larger increases. As a result I am glad to say that I have been able to provide, after account is taken of expected receipts for the local authorities, the Housing Corporation and the Scottish Special Housing Association to have programmes at or above this year's level. Total gross capital expenditure will be about £540m.

On capital expenditure generally, about £420m will be available for local authority capital programmes apart from Housing, also after taking account of expected receipts. This is about £15m more than the comparable planned figure for the current year. About a further £380m will be available for the central government capital programmes, including health, Trunk Roads and investment by the SDA and HIDB. All in all this amounts to a gross capital programme of about £1,340m, the bulk of which will be spent on construction projects.

A feature of capital expenditure is the tendency for provision to be underspent. I have already taken measures to minimise underspending this year: I have removed all limits from spending by housing authorities this year on improvement and repairs grants and supplementary consents of £17m were given to local authorities in respect of other services. I hope that these measures will ensure an outturn for 1982-83 that will be well up to the plan and we shall similarly be making every effort in 1983-84 to see that the provision that we have made for capital programmes is fully utilised.

3 DEC 1982

10 DOWNING STREET

Prime Minister

Long Term Public Expenditure

I asked the Treasury what their objectives were for your meeting on [illegible] Tuesday with Mr Fowler, on long term public expenditure options.

With the Chief Secretary's agreement they sent me the attached copy of his brief for the meeting.

You may also like to glance at the minutes of the Sept 9 Cabinet, to see the assumptions underlying Scenario A and B (under the latter, public expenditure would rise to

47% of GDP if no action

is taken).

MCS 13/12

LONG TERM PUBLIC EXPENDITURE: SOCIAL SECURITY

Social security is the single largest public expenditure programme. At a planned £34 billion in 1983-84, it represents over one-quarter of public expenditure. (The attached table shows how this total cost is broken down between the main benefits). Clearly this programme cannot be exempted if there is a serious commitment to contain the growth of public expenditure over the next 10 years.

LTPE Study

2. The study by officials in ~~LTPE~~ the Long Term Public Expenditure Study made the following estimates of expenditure on social security:-

	1979-80	1982-83	1990-91 Scenario A	1990-91 Scenario B
£m (1980-81 cost terms)	22,878	26,646	28,560	27,320
% GDP	9.6	11.3	9.7	11.1

3. In fact, the 1983-84 total of £34 billion equates to £27.3 billion in 1980-81 costs; in other words, the programme has already reached the level forecast under Scenario B. Moreover, the LTPE projections are on a conservative basis; Scenario A assumed a 1 per cent per annum growth in the real value of existing benefits (but no other improvements) and Scenario B no real increase. The current debate over the overshoot in this year's uprating illustrates how precarious these assumptions are. In both Scenarios benefits are assumed to fall relative to wages. It should also be noted that over the decade demographic factors are not unfavourable. The number of pensioners does not increase significantly. The Scenario B unemployment was assumed to fall to 3m by 1990-91, and in Scenario A to 2m. If unemployment were to increase further, then expenditure would be that much higher: the 1983-84 figures quoted above assumed unemployment at 3.2 million but a variation of 100,000 in the unemployed is estimated to vary benefit costs by about £220 million.

Possible Measures to Contain Expenditure

4. Possible means of restricting the growth of the programme include the abolition of one or more major benefits or severe restrictions on eligibility. Neither seems practicable on the major scale that

would be needed to make an impact on the level of expenditure. The alternative is to alter the uprating arrangements so that the Government is no longer statutorily obliged to uprate most benefits in line with inflation.

De-Indexation

5. The broad choices in this projected study lie between on the one hand constructing a legislative formula which would detach benefit uprating from prices (either over the long term or in certain defined circumstances) or allowing Government flexibility in determining the uprating (with or without some indication in the legislation of the factors which would need to be taken into account). The study should cover the various possibilities under each approach.

Pledges

6. It should be noted that while legislation is essential, it is by no means all that is required. Whatever the decision on the form of the legislation, savings would not be achieved over the medium term unless future Governments adhered to the same objectives in their uprating policies. For instance this Government has pledged full price protection of pensions and linked long-term benefits (accounting for 60 per cent of expenditure), although there is no statutory duty to do so, and notwithstanding that there is no statutory requirement or even a pledge to uprate other benefits such as supplementary benefit and child benefit at all, it has been the practice to uprate them in line with inflation.

Possible Savings

7. These are potentially very large. For example, a 5 per cent cut in the real value of all benefits would save about £1½ billion in 1990. But of course the exact size of the savings will depend on decisions taken by future Governments each year between now and then.

Overshoot and Undershoot

8. MISC 88 is examining separately the question of the form of the legislation required to carry into effect the decision that next year's

benefit uprating should be adjusted to reflect the over-provision this year. As now envisaged, this would be a separate exercise; this session's legislation would simply allow the Government to take into account overshoot as it is already able to take into account undershoot in deciding upon an uprating but would not go any further in the direction of de-indexation.

Social Security Expenditure: 1983-84 - By Main Benefit

Retirement Pension	13,543
Unemployment Benefit	1,850
Invalidity Benefit	1,838
Supplementary Benefit	5,225
Child Benefit	3,916
Housing Benefit	2,085
Other	4,608

LONG TERM PUBLIC EXPENDITURE: HEALTH AND PERSONAL SOCIAL SERVICES

Long Term Public Expenditure Study

The study by officials on LTPE made the following estimates of expenditure on health and personal social services (net of charges):-

	1979-80	1982-83	1990-91 Scenario A	1990-91 Scenario B
£m (1980-81 cost terms)	10494	11341	14110	13330
% GDP	4.4	4.8	4.8	5.4

Economic Scenario A was optimistic, described as "not far short of the best we can expect".

Scenario B was much less favourable.

2. The main reason for the expected real growth in expenditure is that demographic changes (especially the rising number of very old people) require increases in expenditure of about 0.7 per cent a year to maintain standards. DHSS also argue that increases of 0.5 per cent a year are necessary as a contribution to the costs of medical advances if they are to be met without reducing standards elsewhere. The LTPE work therefore assumed (allowing also for an offsetting increase in efficiency) that the real growth in provision after 1984-85 might be 0.5 per cent a year in Scenario B and 1.5 per cent a year in Scenario A. No substantial allowance was made for increasing charges.

Study of Alternative Health Finance

3. This study, by officials and private sector consultants, completed at the end of 1981, listed three possible strategies for the future financing of health care:-

I. Continuation of the present tax-based system, but with possible major changes to the way services are provided and with increases in charges.

II. Replacement by a social insurance system (employers and employees to pay for health insurance rather as they already pay in this country for national insurance).

III. Replacement by a private insurance system.

In July, health departments' Ministers, and the Chief Secretary discussed how to proceed with further studies of strategy I. It was agreed then to study the scope for:-

a. Raising more income from charges;

b. Privatising some parts of the NHS, particularly the General Ophthalmic Dental and Pharmaceutical Services;

c. Reducing demand for treatment by charging patients the full cost of services received and reimbursing them subsequently (on the lines of the system used in France);

d. Giving further encouragement to the private health sector through fiscal concessions.

Possible Savings

4. Treasury estimates made earlier this year, not agreed with DHSS, suggested that higher charges might raise £300m or more a year and privatisation of the dental, ophthalmic and pharmaceutical services about the same amount. The effect of c and d above is very difficult to quantify.

Progress So Far

5. Work on the studies which were decided upon in July was held up while the papers on long term public expenditure were being considered. There is now no obstacle to their being pursued in earnest. They would be private, internal studies, which could be carried out without any effect on industrial relations.

6. Other current work which is relevant to the Cabinet remit includes the numerous initiatives on NHS efficiency, and the move to promote increased contracting out of NHS function. These are going ahead separately.

Line to Take

7. You are recommended to tell Mr Fowler that you see vigorous pursuit of the July studies as the main way of meeting the remit on LTPE.

From: M J C [illegible]
Date: 2 DECEMBER 1982

1. MISS KELLEY

2. CHANCELLOR OF THE EXCHEQUER

cc: Mr Hart
Mr Sallnow-Smith
Mr Sargent

copies attached for:

Chief Secretary
Sir D Wass
Sir A Rawlinson
Mr Mountfield

LONG-TERM PUBLIC EXPENDITURE: EDUCATION

This is a brief for the Prime Minister's meeting on 7 December with Sir Keith Joseph, which the Chief Secretary is also to attend. You have Mr Mountfield's general brief of 26 November.

2. Officials' original report on long-term public expenditure showed that, on present policies, education spending would fall both in cost terms and as a percentage of GDP by 1990, because of demographic change. We need these savings anyway. They do not exempt Sir Keith from the need to find more. Nor can we afford to redeploy them on other educational initiatives - as Sir Keith sometimes appears to believe.

3. The CPRS paper identified three options in the education field:-

- cutting teacher numbers (£1 billion a year)
- charges for schooling (£3-£4 billion)
- charges/loans for students (£1 billion)

Our original briefing on these is attached. Sir Keith is not of course confined to these. You will want to encourage him to pursue any promising variants or alternatives.

4. The risk in the higher education sector is that Sir Keith will regard the DES remit as overtaken by:

a. the DES work on a much less radical student loans package.

b. A more recent remit to CPRS from the Prime Minister on the effectiveness with which the higher education sector meets the needsfor industry.

5. While both pieces of work are important, they do not let the DES off the hook. The DES student loan options save only £200 million a year and that probably not within this decade. The CPRS remit on higher education is more about efficiency than public expenditure savings. Of course its results may well provide pointers to areas where savings could be made but it cannot b e guaranteed to yield the magnitude of savings the LTPE exercise is looking for.

6. So you will want to press Sir Keith to look beyond the work which is already in train. Not least, you will want him to think seriously about the possibility of a more far-reaching loans scheme than he is currently considering.

7. As for the schools field, our briefing on the CPRS "Charging for Schooling" proposal referred briefly to vouchers. You are familiar with Sir Keith's subsequent proposals for a watered-down pilot scheme, which envisaged increased public expenditure. In his paper Sir Keith considered but rejected largely on political grounds the introduction of a market-based school system similar to that described by CPRS. In further discussion of his scheme you may be able to beef up the pilot proposal a bit. But whether or not you succeed in this, you will want to encourage Sir Keith to consider in the LTPE context the possibility of a more thorough-going market approach. Such a system holds out the prospect both of generating substantial revenue through school fees and of drastically scaling down (if not abolishing) the local education authorities, many of whose functions would be rendered superfluous.

8. We doubt whether Sir Keith can offer up substantial savings other than those set out in the CPRS paper (or variants on those) except by way of a package of smaller items. This might for example include two options produced (but rejected) during the

recent Survey: the abolition of provision for under fives and the abolition of the school meals service with the introduction of a shorter school day, saving around £130 million and £220 million respectively in a full year. But measures such as these would arguably give rise to controversy quite out of proportion to the (relatively) modest savings.

Conclusion

9. You will therefore wish to urge Sir Keith to take this exercise seriously. It is not your intention to tell him how to make long-term savings in his programme. Any option is likely to be painful and difficult. But the same will no doubt be true of the options for other programmes. You hope therefore he will not be persuaded that work he has already set in hand disposes of the need for a radical look at his programme.

MF.

M J C Faulkner

CUTTING EDUCATION SPENDING

Background

1. Inputs into school education (eg as measured by pupil/teacher ratios) have rocketed since the war. The effect on qality of output is at best debatable. Recent attempts to rein back have been defeated by lack of controls over LA current spending and LA's reluctance to cut back the teaching force and close down surplus capacity in line with falling rolls.

CPRS proposal

2. As an alternative to charging (Annex G) they propose to cut (say) £1 billion off schools expenditure by concentrating on 'core' subjects, getting rid of unsatisfactory teachers, and exploiting inform ation technology.

3. This would be fine if the cuts could be managed in such a way as to preserve quality of output. But:

- the cuts would be undeliverable under the present LA financia régime

- even if deliverable they might not fall in the right place. The youngest and best teachers - with the best prospects elsewhere - might be the first to leave. Those that remain would not necessarily be qualified in the right mix of subjec And authorities might continue to resort to easy short-term expedients such as cutting book provision and maintenance rat than tackling fundamental problems of over-capacity.

Line to take

4. There is no doubt substantial scope for cutting schools expenditu without serious damage to the system. But the overall problem of conta ing LA current spending would first have to be solved. Even then autho ities would not necessarily deploy their reduced resources in the most efficient way unless market pressures could be brought to bear more effectively (which takes us back to Annex G). At least until we are clearer where we are going on LA expenditure controls generally, this not seem to be one of the stronger candidates for review.

ANNEX G

CHARGING FOR SCHOOLING.

Background

1. Schooling is currently compulsory for 5-16 year old children and, in state schools, free for children of all ages.

CPRS proposal

2. Schooling for a specified age-group would still be compulsory. But full cost would be charged subject to:

- some form of support for poor parents;

- some system to compensate for inescapably high unit costs of eg inner city schools.

Savings would be up to £3-4 billion.

3. Efficiency gains should be expected as a result of increased competition between public sector schools and fairer basis of competitio between public and private sectors. (But transitional problems of self-reinforcing run-down in unpopular schools could be severe). A voucher scheme would have the same effects but would mean an increase in public expenditure. But political difficulties where authorities were reluctan to impose adequate fees. A problem not sufficiently stressed by CPRS is that fees for compulsory age schooling would be seen as tantamount to a new tax.

Line to take

4. In view of the potential savings you will presumably want to press for this option to be seriously examined. But you may get little support. In that case, you could seek a much more limited study of charging for under-fives and over-sixteens - both at school and in FE institutions. (DES recently tried and failed to get agreement to legislation ruling out charging in FE institutions on the grounds that comparable provision in schools was free).

ANNEX H

CHARGING FOR HIGHER EDUCATION

Background

1. At present, higher education institutions are 90% funded by grants (via UGC etc) and only 10% by tuition fees. Most students get mandatory awards, which cover fees in full, and maintenance on a means-tested basis.

2. Proposals are already being developed for replacing the maintenance element of student awards, or a proportion of this, with loans. The DES version would ultimately save £200 million a year; more radical variants seem possible.

CPRS proposal

3. CPRS are suggesting:

- 100% of institutions' costs would be met by fees (and any private money they could raise);

- only a limited number of students would have their fees paid by Government, or have access to a Government loan scheme.

4. This would save possibly £1 billion a year and should make both institutions and students more market-oriented in their behaviour. Possible objections are that it would give the institutions a very bumpy ride (so they will fight it tooth and nail); could lead to some reduction in the supply of needed graduates; and could give an unwanted boost to arts courses because these are much cheaper than science ones - though job market signals would still point firmly the other way.

Line to take

5. Well worth detailed examination. We should not be deterred by predictable opposition from vested interests - however articulate and influential. Mounting review does not of course commit us to action at the end of the day.

LONG TERM PUBLIC EXPENDITURE: DEFENCE

This note offers advice for the meeting with the Defence Secretary to discuss the implications for the defence budget of reductions in long term public expenditure. Your objective will be to secure agreement to the CPRS proposal for defence spending.

... 2. The LTPE assumptions for defence spending are at Annex A. In brief it was assumed that defence expenditure would increase each year by 3% in real terms until 1988-89, and thereafter by 1% each year in real terms. No account was taken of additional expenditure in respect of the Falklands.

... 3. The CPRS proposal for defence spending is at Annex B. In brief, it was proposed that defence expenditure cease to increase in real terms after 1985-86. Thus the CPRS in no way advocated a cut in defence spending (in contrast to other programmes); in recommending it be held at its 1985-86 level they were suggesting an annual spend "only" 9% higher in real terms than in the current year.

4. MOD were never happy about the presentation or the moral of the LTPE figures. For the September Cabinet discussion, Mr Nott circulated his own memorandum - C(82)33 - which concluded, "It is not defence expenditure which needs curbing ... but public expenditure generally, if that can be done." Mr Nott believed that defence ought to be accorded "around 15% of total Government expenditure"; that is, about £2bn more than has been provided for 1983-84.

5. It is not clear whether, following Cabinet decisions on LTPE (CC(82)41st Conclusions), Mr Nott accepts that his budget must play its part in overall reductions; or whether he still holds that defence
... spending should be absolved from any further review. Annex C discusses the sort of arguments the Defence Secretary might deploy for ignoring LTPE considerations and maintaining growth in the defence budget. The main one could be to quote the NATO target; but this is not meaningful, and ought to be replaced by something better.

The Case for the CPRS Proposal

6. As Sir Robert Armstrong said in his minute of 23 November, if the exercise as a whole is to achieve anything significant, the "big four"

/ programmes,

programmes, which account for two-thirds of total expenditure, must contribute their share. It will be difficult enough to achieve LTPE objectives if defence spending merely maintains its 1985-86 level. If, after 1985-86, defence spending continues to increase, the pressur on other programmes will be even more severe.

7. The LTPE exercise is in no sense intended to reopen or lament recent PES decisions. But you may need to remind Mr Nott that defence spending since 1979, and defence expenditure plans until 1985-86, have been largely immune from the public expenditure and economic pressures that have beset other programmes. The Government has not only stood by its commitment to plan for 3% real growth each year at a time of declining GDP; it has recently agreed, on top, defence Falklands additio of some £3 billion over the PES period. The Defence Secretary ought reasonably to accept that this process cannot continue indefinitely without intolerable strain on public expenditure and/or the economy. Some general discussion of UK defence expenditure is at Annex D.

8. The great advantage of the CPRS proposal for defence is its ready feasibility. It does not run against the existing commitment to plan for 3% growth up to 1985-86. Moreover internal MOD planning, in their Long Term Costings, - Falklands apart - currently assumes exactly the CPRS path of future provision. So there should be no adverse operational or industrial penalties from disruption of current plans.

9. It also follows that, if it is agreed to adopt the CPRS recommendation, no further LTPE work on defence need be undertaken; internal refinement and adjustment of MOD forward programme can simply continue as usual.

Conclusion

10. It would be possible to exclude the defence budget from LTPE considerations. Defence spending could continue to increase ad infinit at a rate of 3% per annum, with Falklands cash (£3 billion so far) on top. This would either jeopardise the Government's commitment to reduce public expenditure; or severely exacerbate the pressure on other programmes. But our military capabilities would certainly be enhanced; and both the defence industrial lobby and other NATO countries (especially those who are not pulling their weight) would be well pleased.

/ 11.

11. The Government's expenditure and economic strategies however demand some restraint in defence spending. The CPRS proposal is not to cut the defence budget, but simply to maintain it at a level some 9% higher in real terms (Falklands apart) than it is today. This is exactly the level assumed by MOD forward planning. So no disruption should result. Equally, no new LTPE studies need be launched beyond the normal refinement of the forward programme. But it may be for consideration whether efforts should be made to secure a more sensible NATO resource objective than 3% real growth ad infinitum (paras 5-9 of Annex C refer), and Ministers may wish to seek further advice to this end.

DM1 DIVISION
December 1982

Annex A

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

ANNEX B

DEFENCE

Proposal

1. LTPE projections assumed that defence spending would increase in volume terms by 3 per cent a year from 1982-83 until 1988-89, with 1 per cent a year thereafter. The United Kingdom commitment to the 3 per cent growth target currently runs only to 1985-86. The proposal is to maintain the 1985-86 level in real terms, which would save about £1¼ bn a year by 1990-91 as against LTPE. Internal forward planning in the Ministry of Defence currently assumes no growth in the defence budget after 1985-86. Hence this option could be achieved either by providing for no additions to spending at present planned, or by reductions to make room for some inescapable additions, eg by cancelling Trident. But the present planning assumption is deliberately cautious, to allow for some flexibility, so it does not follow that the option could be achieved without affecting milit_ y capabilities.

2. The political and diplomatic difficulties of this option would be reduced if NATO could be persuaded to reduce the 3 per cent target to a level which all or most member countries could realistically be expected to achieve.

Background

3. The present defence base-line is uncertain, in relation both to the level of spending in 1982-83 and to any revisions of plans in the immediate aftermath of the Falkland conflict. But defence spending cannot be ignored in this exercise. It now accounts for about 12 per cent of total public expenditure programmes, and on the basis of the LTPE assumptions (including the assumption that defence prices rise 2 per cent faster than prices generally) it will account for 15 per cent in 1990-91. On these projections, defence is responsible for more than a third of the total expenditure increase (in cost terms) from 1982-83 to 1990-91 - a much larger share than any other programme - though a different base year, or a different assumption about relative prices, would give different results.

Annex B (cont 1)

Arguments in Favour

4.

i. If defence spending is not slowed down, it will continue to rise in relation to GDP, to around 6 per cent on the projection we have taken. Sooner or later, depending on the performance of the economy, this rise is very likely to be found unsustainable, so that drastic cuts will have to be made. It would be more sensible to plan from the outset for a sustainable rate of defence spending, as in the proposal.

ii. In the past a number of other countries have failed to meet the NATO target (even among those with GDP growth rates higher than the United Kingdom), and after 1980 (the last year for which comparative figures are available) their performance is likely to continue to fall short.

iii. The lower expenditure path would be feasible. It would be broadly in line with the forward planning now being undertaken in the MOD (though this deliberately leaves room for flexibility - para 1). Spending with British industry could still be higher than it is today (£6-7 bn per annum).

iv. A lower rate of spend on defence R & D would free scarce resources (high-quality scientists and engineers) for employment in civil R & D.

Problems

5.

i. There would be political problems, international and domestic, in changing course after 1985-86. Last year the United Kingdom supported the NATO Ministerial Guidance extending the commitment to 1988. Present political pressures are for more defence spending, not less.

ii. The absence of real growth in the defence budget, as against the increase in complexity and cost of major equipment, would entail a reduction in United Kingdom military capabilities.

not true: see Annex C para 4

ANNEX C

The case against the CPRS proposal

1. Because the defence programme has not hitherto been planned to exceed the resources implied by the CPRS proposal, the Defence Secretary should not point to any equipment cuts that would be implied. He might choose to emphasise the sorts of equipment (frigates, tanks, aircraft, weapons etc) that he could purchase with more resources than he anticipates. But this is hardly a defence-specific argument; the more money available, the more can be bought.

2. The Defence Secretary will probably wish to refer to the might of the Warsaw Pact threat. Soviet military capability is real enough. But there is no direct correlation between the level of UK defence spending and Russian military might; and the latter needs to be seen in perspective - not least against the Chinese threat and against the economic difficulties facing Mr Andropov. Is it realistic for the USSR or the West to suppose that Soviet military spending will be able to continue regardless of national resource pressures?

3. Another favourite theme is the problem of "cost growth" in defence equipment (this refers to the trend whereby a new generation of weaponry costs more than the old - Tornado more than Canberras, Stingray more than the Mk46 torpedo etc). But "cost growth" is simply a reflection of the increasing sophistication of modern weaponry. Since Tornado is much more capable than the aircraft it is replacing, it is not surprising that it is more expensive. In general, the "cost growth" argument - a simplistic numbers comparison - tends to obscure the far superior capability afforded by sophisticated modern weapon systems. Furthermore, "cost growth" cannot be simply a NATO problem; the USSR is as subject to the expense of modern technology as any nation.

4. In paragraph 5 of his memorandum C(82)33 Mr Nott asserted that the level of expenditure implied by the CPRS (£15-17 billion each year) would lead to a "rapid dimunition of our defence capabilities". On the contrary, with this level of resources each year our military forces could hardly fail to be substantially improved.

/ 5.

5. The main argument against restraining defence expenditure after 1985-86 is that NATO has extended its 3% growth target to 1988-89. It will no doubt be extended again into the next decade. Indeed, SACEUR has recently declared his view (though on what basis is not clear) that 4% annual growth is necessary to meet the Soviet conventional threat.

6. What level NATO spending in general ought to be is not a mathematical exercise. For its part the UK would have a strong case after 1985-86 (when, Falklands apart, defence spending in real terms will be 20% higher than in 1978-79, and will consume nearly 6% of GDP) for simply maintaining rather than increasing its contribution to NATO.

7. A more positive approach would be to persuade NATO to recognise the shortcomings of the arbitrary and simplistic 3% growth aim and substitute something better. 3% rhetoric may well have served its purpose in 1977, when the Alliance (and especially the US) were anxious about resource scarcity. By the middle of this decade however, some more meaningful measure should be used - not least since the less meaningful the target, the less likely it is to be observed. A better yardstick - and objective - might be the proportion of GDP devoted to defence; defence expenditure would thereby be linked with, and not independent of, economic circumstances.

8. The weaknesses of the 3% growth target are as follows:

a) It takes no account of absolute levels of spend (£15bn is a better annual defence spend than £14bn whether or not it involves 3% growth).

b) The target applies simply to all defence expenditure: all expenditure counts - on weapons, on paper clips, on salaries - whether or not it is militarily effective.

c) The target is expressed merely in terms of input. No attempt is made to measure outputs. Gains from improved efficiency or cost-effectiveness are ignored. NATO has repeatedly resisted UK attempts to launch a review to improve the use made of Alliance resources.

d) Performance is measured in simplistic year-on-year terms. The vagaries of one year (eg. higher or lower level of spend) feed through to the next.

9. A useful concomitant of the Longer Term exercise would be to pursue within NATO more effective criteria for members' defence contributions.

Annex D

UK DEFENCE EXPENDITURE.

1. The Defence programme next year will consume about 5.5% o GDP - the highest level since the sixties. It will be higher than education and health for the first time in over 10 years It will consume 13.2% of total expenditure in 1983-84.

2. The UK defence effort already compares extremely favoura with that of our major allies. In absolute terms, the UK defence spend is second only to the US. As a percentage of G the UK is second; in per capita terms third:

	total expenditure 1981 US$ million	% GDP	per capita expenditu US$
US	167,800	5.8	730
UK	25,200	4.9	439
France	23,800	4.2	442
Germany	23,100	3.4	377
Italy	8,700	2.5	151

Source: 1982 Statement on the Defence Estimates
UK figures exclude Falklands expenditure

3. The UK's achievement to date against the 3% target has be good. Mr Nott's memorandum C(82)33 quotes figures based on MOD's internal price methodology. This has been found by the Unwin report to overestimate defence inflation and to understate "volume"; calculations based on the CSO defence procurement deflator show the UK's growth performance to be equal second to the US. The figures are as follows:

	1979	1980	1981 (provisional)	average
US	3.7	5.0	5.7	4.8
*UK	4.7	4.1	1.1	3.3
France	2.5	3.9	3.5	3.3
Germany	1.8	1.9	3.4	2.4
Italy	2.6	4.9	1.5	3.0
**UK	(2.1)	(2.9)	(1.7)	(2.2)

* CSO defence procurement deflator: financial year figures
** MOD price methodology; calendar year figures

4. Moreover, the UK has achieved these increases despite severe economic difficulties. The 1977 NATO Resource Guidance (which formally recorded the 3% aim) recognised that what countries could achieve would depend on their economic circumstances. GDP growth of the principal NATO nations has been as follows:

	1979	1980	1981	average
United States	2.8	-0.4	1.9	1.4
France	3.3	1.2	0.3	1.6
Italy	4.9	3.9	-0.2	2.8
Germany	4.4	1.8	-0.3	1.9
United Kingdom	1.9	-2.1	-2.2	-0.8

Source: OECD

5. UK performance in the future should compare even more favourably. For example provision has been made for real growth of well over 3% (Falklands apart) in 1982-83 and 1983-84. On top of this additions have been made for some £3bn of Falklands costs up to the end of the PES period. It is

/ increasingly

increasingly unlikely that Germany or France, in the light of their economic difficulties, will even attempt to meet the NATO aim in the near future. The US, by contrast, are increasing defence spending, but seem to have abandoned the economic strategy of a balanced budget.

File

bc: Mr. Vereker

10 DOWNING STREET

From the Private Secretary

SIR ROBERT ARMSTRONG

FOLLOW-UP TO CABINET'S DISCUSSION OF LONG-TERM PUBLIC EXPENDITURE

The Prime Minister agrees to the course of action envisaged in your minute to her of 23 November..

We shall accordingly set up a series of separate meetings with the Secretaries of State for Social Services, Education and Science and Defence, together with the other Ministers you mentioned.

M. C. SCHOLAR

24 November 1982

Prime Minister ①

Do you wish to embark on this?

MLS 23/11

Ref. AO82/0227

Yes MT

PRIME MINISTER

Follow-Up to Cabinet's Discussion of Long-Term Public Expenditure

My minute of 7th October (Ref. AO9679) outlined proposals for following up the Conclusions of the Cabinet's discussion of long-term public expenditure on 9th September once decisions on this year's Public Expenditure Survey were out of the way and the controversy over the CPRS Report had died down. Mr Scholar's subsequent minute of 11th October confirmed that you would wish to consider this further after the Public Expenditure Survey had been completed.

2. Now that the Chancellor has announced the main results of the Public Expenditure Survey in his Autumn Statement the way is clear to proceed.

3. My earlier minute (copy attached for convenience) envisaged a two-stage process. The first would be a preliminary round with the Ministers responsible for the four main spending programmes (Social Services, Health, Education and Defence) to consider how the Cabinet conclusions of 9th September might best be carried forward in their areas to produce a reasonable basis for launching the exercise more widely. This first stage which would require the major spending Departments to agree to carry out reviews with the object of making a substantial contribution to reducing public expenditure from within their own programmes, would be difficult, but important: if the exercise as a whole is to achieve anything significant, it is essential that these programmes which account for two-thirds of total expenditure should contribute their shares, and it is crucial that the Ministers concerned should

provide the necessary political will to carry this through.

4. Once that first stage with the main spenders had established a reasonable basis for progress, we could then go on to the second stage, which would be for you to send a minute to the Chancellor of the Exchequer, with copies to all members of the Cabinet, drawing attention to the relevant Cabinet Conclusions of 9th September and asking that reports prepared in consultation with Treasury Ministers and other colleagues as appropriate should be sent to you by the beginning of March.

5. I believe that the Treasury will be content with this way of proceeding.

RA

ROBERT ARMSTRONG

23rd November 1982

File

c. Mr Gregson
Mr Buckley

Ref. A09679

PRIME MINISTER

CABINET OFFICE
A ....
31 OCT 1982
FILING INSTRUCTIONS
FILE No. ....

Follow-up to Cabinet's Discussion of Long-Term Public Expenditure

The conclusions of the Cabinet's discussion of long-term public expenditure on 9 September invited all Ministers with responsibility for public expenditure to review their programmes critically with a view to contributing to a substantial reduction in public expenditure in the longer term; to discuss their proposals with Treasury Ministers and other colleagues as appropriate; and to report (CC(82) 41st Conclusions, Minute 4). The intention was that any further work on long-term public expenditure should be under close political supervision by the spending Ministers concerned.

2. I imagine that you will want to get decisions on this year's Public Expenditure Survey out of the way, and also let the dust settle on the controversy over the CPRS report, before taking any initiative to follow up the Cabinet's conclusions on 9 September. Assuming that this year's public expenditure round has been completed by late November, it would then be timely to see what could most usefully be done to ensure that spending Ministers are, while recognising the political sensitivity of the issues, examining critically their long-term programmes.

3. As you know, two-thirds of public expenditure is accounted for by four programmes (social security, health, education and defence) for which, apart from the territorial Ministers, three Ministers are responsible, the Secretaries of State for Social Services, Education and Science and Defence. The exercise will achieve little without a political will on the part of those Ministers. It would also be desirable that you, Treasury Ministers and the spending Ministers concerned with those programmes should be broadly agreed on the political framework within which any further studies should be carried out.

4. This suggests that the best way of proceeding might be in two stages, as follows:

(i) As soon as this year's Public Expenditure Survey is out of the way, you, together with the Chancellor of the Exchequer and the Chief Secretary (and perhaps the Home Secretary) might have a series of separate meetings with the Secretaries of State for Social Services, Education and Science and Defence to consider how the Cabinet's conclusions of 9 September might best be carried forward in their areas.

(ii) Assuming that a reasonable basis for progress can be established in those areas, you might then set the exercise in train generally with a minute to the Chancellor, copied to all members of the Cabinet drawing attention to the relevant Cabinet Conclusions on 9 September and asking that reports prepared in consultation with Treasury Ministers and other colleagues as appropriate should be sent to you by the beginning of March. The aim would be to discuss the reports between the Budget in mid-March and, say, end-April when next year's public expenditure exercise will be put in hand. You might wish at that stage to set up a small group of Ministers to consider the reports rather than have them put to the full Cabinet, but that decision could be deferred until we had a better idea of what the reports would be likely to look like.

5. In your summing up of the Cabinet's discussion on 9 September you said that there were also "potential areas of study which affected several Departments and might therefore better be conducted centrally" and that you "would give further consideration to how such studies might best be organised". I am assuming that you do not want to have any specific action taken about that at this stage.

ROBERT ARMSTRONG

7 October 1982

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CONFIDENTIAL

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JU111
Secretary of State for Industry

9 November 1982

The Rt Hon Norman Tebbit MP
Secretary of State for Employment
Caxton House
Tothill Street
London SW1

Prime Minister (2)

MLS 9/11

Dear Norman,

Today's debate in the House on public enterprise, in which both you and I will be speaking, will afford me the opportunity to announce that the four-months deferment in payment of Regional Development Grants is to end immediately. I shall also announce that Jim Prior will be ending deferment as it applies to the Standard Capital Grants Scheme in Northern Ireland.

2 This measure will bring forward for payment the £150 million in grant payments which is currently held in deferment. I hope that the deferred payments can be cleared within a month. New applications, and those under consideration, will not be subject to deferment and should not experience significant delay whilst the RDG Offices deal with the many thousand deferred payments.

3 In making the announcement, I shall refer to the introduction of deferment in June 1979 and say that, whilst it was necessary and important at that time, we have been aware that its continuation involves an unwelcome extra financing cost to industry.

4 This measure will be warmly welcomed by industry. It will give a valuable boost to company liquidity in the manufacturing sector and act as a further incentive to those companies who are already investing in areas where need is greatest.

5 I am copying this to the Prime Minister, Geoffrey Howe, Peter Walker, Michael Heseltine, John Biffen, David Howell, Norman Fowler, Janet Young, Nigel Lawson, Cecil Parkinson and Arthur Cockfield.

Yours

Patrick

The Economy

3.30 pm

The Chancellor of the Exchequer (Sir Geoffrey Howe): With permission, Mr. Speaker, I should like to make a statement.

As the House knows, it is customary at this time of year to publish outline public expenditure plans and proposed national insurance changes for the year ahead, together with the economic forecast required under the Industry Act 1975. This year, as foreshadowed in the Government's reply to the report of the Treasury and Civil Service Select Committee on budgetary reform, we are bringing these together and publishing them in an autumn statement which I shall today be laying before the House. I am grateful to my right hon. Friend the Member for Taunton (Mr. du Cann) and the Select Committee for the initiative which has led to that development.

During the past year, monetary conditions have exerted downward pressure on price rises and substantial progress has been made against inflation. In January the rate of inflation was 12 per cent.; it is now around 7 per cent.; and we envisage a 5 per cent. rate early in 1983. Interest rates have fallen even more sharply, with bank base rates down a full seven points from their peak of 16 per cent. last year to 9 per cent. today. The CBI has calculated that each percentage point fall benefits British industry by around £250 million in a full year. We shall continue to maintain downward pressure on the monetary aggregates to achieve further success in the battle against inflation. Interest rates will continue to reflect the indicators of monetary conditions which I described in my Budget speech.

As the statement explains, the growth in output this year—in this country and throughout the Western world—has been lower than anticipated. For next year the Industry Act forecast now suggests a 1½ per cent. increase in our GDP. That is close to what is expected for most other industrialised countries. Unemployment remains the nations's most distressing problem. As in other countries, further rises are expected to continue into next year, although they should moderate as output picks up in response to lower inflation and lower interest rates.

Public borrowing remains under firm control, which of course is one reason for the fall in interest rates. We expect the PSBR this year to be within the figure of £9½ billion expected at the time of the Budget. Final decisions about the level of next year's borrowing requirement will not of course be taken until my 1983 Budget. The current forecast suggests that the scope for possible tax reductions in 1983-84 could be of the same order as was indicated at the time of the last Budget. That is on the basis of conventional assumptions as to the revalorisation of direct taxes and excise duties. It also assumes the same 1983-84 PSBR, as a percentage of GDP, as was assumed at the time of the last Budget, and takes account of the decisions which I am announcing today.

The public expenditure planning total for 1983-84 will be £120·06 billion. That is lower than the provisional figure for 1983-84 published on Budget day this year. It is the first time since 1977 that a Government have been able to stop expenditure plans for a particular year rising with each annual review. Compared with the plans for the current year, the new total is a slight fall in cost terms—that is, in constant prices. The ratio of public expenditure to GDP will come down from 45 per cent. to 44 per cent.

Details of the changes in individual programmes are summarised in the statement. Social security programmes have been adjusted to take account of the rapid reduction in inflation. This month's benefit uprating is 11 per cent. Even allowing for the 2 per cent extra to compensate for last year's shortfall, that is well over the current rate of inflation. We accordingly intend to make an adjustment to next year's uprating. Meanwhile, those in receipt of benefits will continue to receive payment at a rate above that needed to compensate for price rises in the last year. As is customary, the exact size of next year's uprating will not be decided before Budget time.

The House will be glad to hear that the resources that we had planned to make available for a number of important programmes have been increased. We plan additional gross expenditure of £260 million on two new special employment measures—the community programme and the job splitting subsidy—which were announced earlier this year. For housing, the provision of an extra £49 million and a continuing high level of receipts from council house sales will allow gross capital spending to be at least 10 per cent. higher than the expected level this year.

More money will be made available for the urban capital programmes to support the new urban development grant programme and the urban development corporations in London docklands and Merseyside. These two changes represent a significant new boost to the construction industry.

In addition, £96 million more has been allocated to law and order programmes, mainly on police and prisons. In the Health Service we are providing an extra £80 million in England, which should continue the growth in the level of services that has already taken place under this Government. Comparable increases will be made for the rest of the United Kingdom.

Finally, provision for defence in 1983-84 has been increased by £622 million because of extra costs following the Falkland Islands action. That increase is over and above our commitment to meet the NATO 3 per cent. per annum real growth target. It will fund purchases of equipment to replace losses this year and will ensure the future security of the Falkland Islands.

To find room for these increases within an unchanged total, we have been able to secure economies elsewhere. We have also transferred to programmes part of the provisional contingency reserve set aside in the 1982 White Paper, but we have left a substantial contingency reserve of £1·5 billion, which we shall review again nearer the Budget.

Full details of public spending plans for next year and for 1984-85 and 1985-86 will be set out in the public expenditure White Paper which we expect to publish early in the new year.

My right hon. Friend the Secretary of State for Social Services is this afternoon announcing details of changes in national insurance contribution rates and limits for next year, and will be publishing the report of the Government Actuary on the national insurance fund. If we were fully to balance the fund for next year, increases in employers' and employees' contributions of nearly 0·4 per cent. each would be required. But we are anxious both to minimise additional burdens on industry and to diminish the effects

[Sir Geoffrey Howe]

of contribution increases for employees, so we have decided that the increases should be limited to 0·25 per cent. each for employers and employees. The upper earnings limit will go up only to £235, rather than £245 which would be the maximum permitted by statute.

Taken together, these measures mean that contributors will pay a little over £200 million less next year than would have been required fully to balance the fund. The cost to the PSBR has been taken into account in the forecast.

I turn now to the national insurance surcharge which was introduced and then increased to 3½ per cent., by the previous Government. It has long been criticised, and rightly so, by commerce and industry. As I said in my last Budget statement, it raises production costs, it is not rebatable on exports, and it either puts up prices or cuts into profits.

I was able in March to announce an effective reduction of 1 per cent. in the rate for private sector employers, from 3½ per cent. to 2½ per cent., for the year 1982-83. I am pleased to inform the House that we can now take another substantial step in the right direction, by reducing the rate for 1983-84 by a further 1 per cent., so bringing it down to 1½ per cent. The cost of this to the PSBR has been reflected in the forecast.

The public sector will not gain from the change, but the benefit to private employers in 1983-84 will be around £700 million. Overall, this will more than offset the increase in their costs due to the new NIC rates and levels. A table showing the overall effect for employers and employees of the NIC and NIS changes for next year has been put in the Vote Office today.

That is not all. I intend that for private sector employers ½ per cent. of the NIS reduction from April 1983 should be brought forward and made effective for 1982-83 also—that is to say, for the current year. Hon. Members will know that to change the NIS rate at this time of year presents considerable administrative problems, but we have found a way of overcoming them. The equivalent of a ½ per cent. reduction for the whole year will be given by reductions in employers' payments of national insurance surcharge and national insurance contributions for January, February and March next year. Details and guidance will be sent in due course to employers.

That further benefit will be worth £350 million in the current year. Legislation will be needed for the new arrangements both this year and next. A Bill will be introduced at an early date. I am sure that it will commend itself warmly to the House as providing a substantial reduction in the costs faced by private sector commerce and industry.

The House will want to study the autumn statement carefully. The format is new and, I hope, helpful and the scope rather wider than before. It demonstrates that we are determined, within the framework of our monetary and fiscal policies, to continue to do what we can to relieve the burden of taxation so as to move towards renewed growth and more employment. I hope to be able to say rather more if I am fortunate enough to catch your eye, Mr. Speaker, later in the course of our current debate.

Mr. Peter Shore (Stepney and Poplar): The Chancellor has made a long statement. It is as full of information and documentation as it is remarkably empty of any promise or hope for the British people or for the rescue of our savagely damaged economy after 3½ years of the Chancellor's regime at the Treasury.

It is a depressing statement. It marks the fact that we have often brought to the attention of the House—the failure of the strategy and judgment of this year's Budget. It also marks the failure of the past 3½ years of Government economic policy. The Government's Budget was based on the premise that there would be an upturn and a bottoming out of the economy. The Opposition said that that would not happen. The Chancellor has now had to confess that the rate of growth in Britain in the past year has been 0·5 per cent. We all know that we are in the middle of a massive recession. The Chancellor has done virtually nothing, apart from a couple of cosmetic touches to the national insurance surcharge, to face that challenge.

I have several questions to ask the Chancellor. The first relates to what he said about the adjustment to next year's uprating of old-age pensions. Is he aware that the cost of not adjusting that uprating will be only £250 million during the present fiscal year? Is he further aware that the cost for a full year would be only £500 million? Is he aware that the cost of living affecting retirement pensioners and most people on low incomes is much higher than the proposed increase because their pattern of expenditure is different from that of the rest of the country?

It is monstrous for the Chancellor to claw back from people, the great majority of whom are having a more difficult time than they can recall, this year's so-called overpayment. Can he justify making yet another major statement and failing to make good the 5 per cent. that was taken away from the unemployed? The Chancellor said that he is worried about the number of unemployed. It is a scandal that so many people should be made unemployed, but, having made them unemployed, he takes away a substantial part of their benefit. What type of generosity is that?

I shall now deal with the changes in the national insurance surcharge. I had hoped that, at the very least, the Chancellor, if he cannot bring himself to do anything else to assist British industry, would have removed the national insurance surcharge in next year's Budget. He said that, apart from a relatively small, once-and-for-all three months' cash injection in the first quarter of next year, the net result would be that, minus the increased employers' national insurance payments, the cash flow of firms throughout Britain will be no more than £175 million higher than it is now. I should be grateful if he would confirm that. I believe it to be the case.

I turn now to a rather surprising omission from the Chancellor's long statement. He said nothing about the rate support grant for the coming year. Last year we were told what the percentage rate support grant would be. We were also told of the anticipated increase in council house rents. What are the present estimates for both those important items? They are important because unless something is done about rate support grant ordinary people and industry will face more increases in rates next year.

I shall conclude with three questions. The first relates to unemployment. The Chancellor has already made it plain in the document that accompanies his statement that the unemployment assumption is to increase from the 2·9 million of this year to no less than 3·2 million next year. As the Chancellor believes that he has reduced inflation to single figures, can he tell us when the economy will take

on the predicted orderly, natural and spontaneous growth upon which the whole of the Government's policies are predicated?

Secondly, will the Chancellor confirm that personal living standards are now running at 3½ per cent. below what they were when he took office in 1979? What is his assumption or forecast for living standards for next year?

Thirdly, having examined the industrial forecasts that accompany the Chancellor's statement and having noted that the balance of trade is expected to deteriorate—although it is not quantified—I should like to know whether Britain, for the first time in recorded history, is importing more manufactured goods than it is exporting to the rest of the world?

This statement comes after three and a half years of Conservative Government, and covers the prospects for the last year of a five-year Parliament. It builds upon a record of failure, offers no prospect to the country, and shows that the Government have not even begun to understand what is needed to tackle the problem that they face.

Sir Geoffrey Howe: The right hon. Gentleman began with a caricature of the economic improvements that have taken place in recent years. Am I to take it that he brushes to one side the prospect of inflation down to 5 per cent.—a formidable and important achievement? Am I to take it that he brushes aside a fall in interest rates of 7 per cent., which would not have been achieved without firm control of public spending and borrowing for which we received little support from him?

The right hon. Gentleman drew attention to the unemployment assumptions that are set out in the autumn statement and the Government Actuary's report. They show an average increase next year of 300,000—from 2·9 million to 3·2 million. As I said in my statement, that rate of increase is likely to decrease as the year goes on.

The right hon. Gentleman asked about council house rents. The autumn statement shows that the Secretary of State for the Environment will be consulting the local authority associations on a rent increase of 85p per dwelling per week. If that figure is confirmed, it will mean no increase in real terms in 1983-84, and it will enable us to provide for a real increase in housing capital investment that year. I hope that the House will welcome that.

The right hon. Gentleman also asked about the rate support grant. The announcement of the provisional figure has already been made by my right hon. Friend the Secretary of State for the Environment. Consultation is taking place on that, and I have nothing further to add.

As to the adjustment in pensions, the pension increase provided for in this year's Budget not merely provided fully to make up for the 2 per cent. shortfall in the preceding year but also, as it turns out, for more generous provision for price increases than those that have taken place this year. If we are to maintain real value in that sense, it is bound to mean adjustments from year to year, just as we have experienced in successive years. There is nothing extraordinary about that, and I assure the right hon. Gentleman that the pledges are being maintained.

With regard to living standards, the right hon. Gentleman should by now understand that one of the causes of our economic difficulties was the substantial increase in real personal disposable income that took place between 1977 and 1980 as a result of the wage explosion that concluded the disastrous period of office of the Labour Government. To some extent, that increase has been reversed, but there is still further need, as the right hon. Gentleman pointed out, for improvements in our competitiveness if we are to expand our rate of growth and increase our share of the domestic market. In fact, in the current year, real demand in the economy has increased by 3 per cent. We shall get a larger share of that for British manufacturers and exporters by continuing to improve our costs. I hope that I shall have the unqualified support of the right hon. Gentleman for the need for continued moderation in pay settlements if that is to be achieved.

The last feature is the need to reduce the overall cost burden falling on employers. By wringing his hands in horror at the reduction in the rate of national insurance surcharge, the right hon. Gentleman astonished and amazed the House. As a result of the changes in national insurance contribution and national insurance surcharge, the total reduction in the cash burden on employers in the next year will be £686 million, about £450 million of which will be a reduction wholly to the benefit of the private sector.

I hope that the House will be struck by the contrast between this Government's record, who, by taking national insurance contribution and national insurance surcharge together, have effected a reduction in the combined burden of 1½ per cent., and the record of the Labour Government, who, in spite of the right hon. Gentleman's hypocrisy today, increased the joint burden of those taxes by 5 per cent.

Mr. Shore: The Chancellor replied in his own way to my question about what had happened to living standards and confirmed that they had fallen. I asked about the prospect for the coming year based on his own estimate. I should like an answer to that question.

The question of competitiveness relates very much to the national insurance surcharge. The case for getting rid of the national insurance surcharge is to increase the competitiveness of British industry. Will the right hon. and learned Gentleman confirm that the loss to Britain's international competitiveness since he took office is still 36 per cent., and what improvement will there be as a result of today's statement?

Sir Geoffrey Howe: The right hon. Gentleman is right to point out that there is still a significant loss of competitiveness now compared with some years ago. He must understand that a large component of that loss was due to the wage explosion that took place under the Labour Government.

As I have already said, real personal disposable incomes for people in work continued to rise almost regardless of economic trends for a number of years, perhaps until a year ago. If we are to secure a further sustainable advance in personal living standards and, at the same time, to achieve a reduction in the number of people out of work—which is surely what all hon. Members would like—it is of crucial importance to continue improving our competitiveness by achieving further moderation in the rate of pay settlements. I should like the right hon. Gentleman specifically to endorse that. I am grateful to him for his welcome for the reductions that we have been able to make in the national insurance surcharge burden that the Labour Government left on British industry.

Several Hon. Members *rose*——

Mr. Speaker: Order. As the content of this statement can and will be discussed today, tomorrow and the day after, I shall allow 20 minutes for questions, which will be very generous. We shall then move on to the next business.

Mr. Roy Jenkins (Glasgow, Hillhead): Does the Chancellor reject the London Business School's forecast that inflation, after falling in the second quarter, will thereafter begin to rise again? What is his own forecast for the fourth quarter of 1983? Would it not have been far more helpful to British industry to have abolished the national insurance surcharge now—a jobs tax clearly perverse in present circumstances—rather than to wait and hope to give personal income tax concessions in the Budget which, because of their unprecedentedly high import content, will have nothing like a similar benefit to the activity in the economy?

Sir Geoffrey Howe: I do not accept the London Business School's expectations for inflation at the end of next year. The right hon. Gentleman will find that my statement says that at the end of 1983 the inflation rate may still be around 5 per cent. I am sure that he will endorse the proposition that if we are to continue to achieve further progress in reducing the rate of inflation at the same time as enhancing employment prospects, it is important to take the main remedy to reduce costs to British industry, which is to achieve further moderation in pay settlements.

I accept that the national insurance surcharge represents an addition to those costs. It is for that reason that I have reduced it by a full percentage point in the current year and intend to do so in the next year. I intend to do that in a way that maintains effective control over the size of public sector borrowing, which is a crucial component in the reduction in interest rates, which in turn is an even more significant element in industrial costs.

Mr. Maurice Macmillan (Farnham): Could my right hon. and learned Friend tell the House how the total employers' share of the contributions to national insurance compares with the share paid by our competitor employers overseas?

Sir Geoffrey Howe: There are wide variations. Taking a very general average figure, it is my impression that employers overseas pay a rather larger sum in contributions of this kind than is paid in Britain in order to sustain social security programmes.

Mr. Jack Ashley (Stoke-on-Trent, South): As the Chancellor of the Exchequer's derisory statement makes it clear that he cannot or will not tackle the scandal of mass unemployment, will he at least provide funds for the payment of long-term supplementary benefit for people who are unemployed in the long term? Would not that be at least a crumb of comfort until we have a Government who are less sanguine about mass unemployment and who are prepared to do something about it?

Sir Geoffrey Howe: I understand the right hon. Gentleman's anxiety about unemployment, and I know that it is genuine and strongly felt. We have to make our choice as to the ways in which we contribute to reducing the burden imposed by unemployment. It is for that reason that I have announced today that £260 million will be devoted to the two employment programmes that I have identified.

Mr. Terence Higgins (Worthing): Will my right hon. and learned Friend note that on the Conservative Benches we do not take for granted the substantial reduction in the rate of inflation and in interest rates? The reduction in the rate of inflation will be very much welcomed, not least by pensioners. I suggest to him that it is essential now to give priority to cutting industrial costs. In that context, will he stress to the Labour Party and the TUC that excessive wage claims, particularly in the public sector—for example, in the water, gas and electricity industries—will further endanger the level of employment if they are persisted with? Therefore, we must take the strongest possible stand against claims for pay increases which are far above the level of inflation.

Sir Geoffrey Howe: I am grateful to my right hon. Friend for his support and welcome for what I have said, and underline the importance of his point. It is crucial to continue to secure a reduction in public sector costs as part of the process of reducing inflation, and a key contribution can be made to that if we achieve moderation in pay settlements within the public sector, in particular in the industries to which my right hon. Friend has referred.

I hope that the Labour Party will find it in its heart to underline and endorse the importance of that message. All too often it is given to complaining about high increases in prices in the public sector utilities, but it is important, if it makes that case, to join us also in arguing the case for a reduction in pay settlements.

Mr. Richard Wainwright (Colne Valley): Does the Chancellor of the Exchequer recall that as an integral part of his Budget statement in March he included a long passage about energy and fuel prices, including the announcement of a gas price freeze, which expires next month? Has he anything to tell the House today on that theme?

Secondly, when the Chancellor referred to modest increases in the housing programme and the community programme, he was wholly specific about the figures, but when he came to the other side of the account he merely said that he was securing economies elsewhere. Will he be equally specific in describing those economies?

Sir Geoffrey Howe: The hon. Gentleman will see the answer to his last point if he studies, as I know he will, the autumn statement produced in response to his representations, among others, as a member of the Select Committee on the Treasury and Civil Service.

With regard to energy prices, the British Gas Corporation has today confirmed that the freeze on the contract price of gas sold to industry will continue until October 1983. That is a matter for the corporation to decide, but it is a decision that it has been able to reach within the agreed external financing limits.

Dr. Jeremy Bray (Motherwell and Wishaw): In view of the omission from the statement of any reference to the exchange rate, is it a coincidence that the rate of reduction of interest rates has been such that the effective exchange rate has not changed? Is not the Chancellor of the Exchequer keeping British industry uncompetitive in order to protect the Government's claim that they have reduced inflation?

Sir Geoffrey Howe: The hon. Gentleman understands that the factors that influence the exchange rate are many and diverse. The assumption made in the autumn statement—it was, of course, presented as an assumption—was that there will be no significant variation in the exchange rate. The hon. Gentleman will appreciate that interest rates in Britain during the past 12 months have fallen by about 7 per cent. compared with an average fall of only 4 per cent. in other countries. He will also have noted the conclusion of the debate conducted by the CBI on the exchange rate in Eastbourne last week.

Sir William Clark (Croydon, South): Is my right hon. and learned Friend aware that all thinking people will not only congratulate the Government on their economic strategy in reducing inflation, interest rates and the national insurance surcharge, but will welcome it? Could he assure the House that he will keep a close watch on public expenditure? Although we welcome the fact that the proportion of GDP has gone down from 45 to 44 per cent., if the Government were to adopt the official Opposition's policy and to increase public expenditure that would put the whole of the economy into jeopardy.

Having given this assistance to industry, will my right hon. and learned Friend, between now and the next Budget, give urgent consideration to reducing the standard rate of income tax?

Sir Geoffrey Howe: I understand my hon. Friend's concern with personal taxation as well as with the tax burden on the industrial and commercial sector, and obviously have that in mind now, as at all times.

I am grateful to my hon. Friend for his support concerning the importance of controlling public expenditure. It is well worth emphasising that all the countries which find themselves facing increasing difficulties, as their public sector borrowing becomes increasingly difficult to control, and as their interest rates and inflation rates likewise become increasingly difficult to control, are those which have not committed themselves to the reduction of the public sector deficit in the way that we have done. It is important for us to maintain and sustain that achievement as a crucial part of the foundation for the restoration of sustainable growth.

I take this opportunity to pay tribute to my right hon. and learned Friend the Chief Secretary for his remarkable achievement on public expenditure, in co-operation and consultation with the rest of our colleagues.

Mr. Harry Ewing (Stirling, Falkirk and Grangemouth): The documents concerning the autumn statement published today contain a passage about old-age pensions. The Chancellor of the Exchequer states there that he is working on the basis of a 5 per cent. inflation rate for next year, less the 2 per cent. overpayment that he claims will be made to pensioners in the next few days. That leads one to the conclusion that the uprating of pensions for 1983-84 will be about 2½p to 3p in the pound. If that is the case, on what basis has the Cabinet taken a decision to make the old-age pensioners pay for the Prime Minister's bungling incompetence in leading us into the Falklands crisis?

Sir Geoffrey Howe: None of the hon. Gentleman's statements is correct. We do not yet know the final result concerning the rate of inflation. The inflation figure for November this year, which is one of the components, is not yet known. By definition, the inflation forecast for next year is not yet known. Those are two components essential to any decision that has to be taken in this respect, which will not be announced until Budget time. Therefore, it is wrong to suggest that the pensioners or any other group are bearing the cost of the necessary expenditure in achieving our national objectives, with the support of the nation, in the south Atlantic.

Mr. Anthony Nelson (Chichester): Does my right hon. and learned Friend agree that, while many of us hope there will be some scope for real improvement in pensions next year, the implications for public expenditure and the burden of taxation would be altogether unacceptable if pensions, benefits and allowances of all kinds were to be uprated only on the basis of forecasts and were unable subsequently to be readjusted when those forecasts proved too modest?

Sir Geoffrey Howe: I entirely agree with my hon. Friend. He underlines the point that I made in my statement.

Mr. A. W. Stallard (St. Pancras, North): Is the Chancellor aware that his statement on the clawback of benefits from pensioners and those on supplementary benefit will be greeted with anger and resentment by millions of people throughout the country? He says that he has been able to make arrangements to adjust the handout on the national insurance surcharge between now and December and January, but pensioners have been asking for many years that their pensions should be uprated nearer the date when the increase is announced so that they do not have to wait nine months for the extra money. Is the Chancellor aware that pensioners will not understand why there can be an adjustment for the national insurance surcharge but not for pensions? The Government have made considerable savings at the expense of pensioners and others in the past three and a half years, and the pensioners' index has been running four or five points ahead of the retail price index for some months. Will the Chancellor reconsider his decision to claw back pensions and to make pensioners pay for other handouts?

Sir Geoffrey Howe: The hon. Gentleman and the whole House must remember the point made by my hon. Friend the Member for Chichester (Mr. Nelson). Benefits to pensioners and others from the national insurance fund have to be paid for out of the fund. That principle was understandably endorsed by the Public Accounts Committee not long ago. Its effectiveness has been manifested by the need, that I have recognised today, for a 0·25 per cent. increase in employees' contributions. That represents a practical limit to the generosity of each member of the working population. Pensioners and other beneficiaries will receive an increase of 11 per cent. this month and will be better off in real terms for the whole of this year. The maintenance of the real value of benefits is bound to mean adjustments from year to year. When we came into office in May 1979 we adjusted the pension upwards by 1·9 per cent. to take account of the shortfall under the Labour Administration.

Mr. Nigel Forman (Carshalton): While welcoming the fact that my right hon. and learned Friend has felt able further to reduce the costs to British industry by about £600 million in a full year, may I ask him to bear in mind the increasingly strong case for further cuts in direct taxation, especially for the lower paid? I am convinced that that would not necessarily lead to a significant increase in the propensity to import.

Sir Geoffrey Howe: My hon. Friend makes the same point as was made by my hon. Friend the Member for Croydon, South (Sir W. Clark). It needs to be taken into account in our consideration of these matters.

Mr. George Foulkes (South Ayrshire): Is not the Chancellor aware that we heard him clearly say that he was adding to the defence budget a sum equivalent to the amount that he is taking away from old-age pensioners? Will he answer the question of my hon. Friend the Member for Stirling, Falkirk and Grangemouth (Mr. Ewing) and tell the House why he has picked on the pensioners to pay for the Falklands war?

Sir Geoffrey Howe: The hon. Gentleman may try as he likes to make a false connection and a false point, but they remain entirely false. The necessity to pay for the Falkland Islands expenditure was recognised by the House from the start to the finish of the campaign. The increase in expenditure in that area will, incidentally, lead to a significant increase in orders for the defence equipment industry, in Scotland as elsewhere. Aside from that, when I have discussed the position of pensioners, I have made it clear that the pattern of changes that we have made is maintaining the pledges that we have so far made to the House.

Mr. Jim Lester (Beeston): I congratulate my right hon. and learned Friend on his timely response with measures that will be helpful to the construction industry and to British manufacturing industry, about which there is considerable anxiety on both sides of the House. Like Oliver Twist, one is always tempted to ask for more and I should welcome an assurance from my right hon. and learned Friend at least on the principle of the restoration of the 5 per cent. abatement of unemployment benefit, if not on the practice.

Sir Geoffrey Howe: That is a matter on which I have nothing to add to what has already been said.

Mr. Barry Jones (Flint, East): Does not the Chancellor's statement signal a continuation of his and the Government's war on the unemployed? Why is he so reluctant to take urgent action on behalf of the communities that are suffering from mass unemployment?

Sir Geoffrey Howe: The Government are not engaged in a war on the unemployed. Like every other Government in the Western industrial world, we are engaged in the difficult and prolonged battle against rising unemployment. As my right hon. Friend the Prime Minister pointed out last week, unemployment has been rising significantly faster in other countries than in this country over the past year or so. The House must recognise, as I am sure that the majority of hon. Members do, that the most effective way of combating unemployment is to continue the success against inflation and high interest rates and, above all, to continue to improve our competitiveness, for which further moderation in pay settlements is crucial, and in that I still invite the support of the Opposition.

Mr. Chris Patten (Bath): May I follow up the question of my hon. Friend the Member for Beeston (Mr. Lester)? Do the public expenditure plans for the coming year include provision for restoring the 5 per cent. cut in unemployment benefit?

Sir Geoffrey Howe: That is a matter which, as I have said already, remains for consideration.

Mr. Michael Meacher (Oldham, West): Will the Chancellor confirm that, even after his package, unemployment will rise to more than 3½ million next year? If he believes that large personal tax cuts will be a significant source of extra demand for domestic industry, and not just an election bribe, how will he prevent more than two-thirds of the extra demand being dissipated on imports, which is exactly what happened last year?

Sir Geoffrey Howe: If that is the hon. Gentleman's analysis, it underlines the importance of improving the competitiveness of British industry and of further moderation in pay increases. I ask yet again whether the hon. Gentleman and the Labour Party endorse and emphasise the crucial importance of moderation in pay bargaining to deal with the problems that he raises.

Mrs. Shirley Williams (Crosby): The Chancellor repeated on several occasions during his statement that unemployment was due to the world recession. Is he aware that the most recent report of the International Monetary Fund says that the British Government have brough about a more restrictive shift in policy than any other Western Government and that one of the two factors responsible for our loss of competitiveness is the Government's restrictive monetary policy? Will he confirm that the reason why he can do so little is that the competitiveness of this country has been reduced by, among other things, the Government's own policies?

Sir Geoffrey Howe: I certainly do not confirm that. The IMF has been commending to all its members the crucial importance of achieving continued success in reducing the burden imposed on the world economy by public sector deficits. We have achieved considerable success in that direction, which is why we have been able to reduce the level of inflation and interest rates as we have. That is the general message which has come loud and clear from the IMF. Other countries ought to listen to the same proposition.

Mr. Hal Miller (Bromsgrove and Redditch): Will my right hon. and learned Friend agree that, contrary to the disappointment felt by the Opposition, the real value of pensions is still being indexed, the lie has been given to the false rumour put about during the Birmingham, Northfield by-election that council house rents would increase by about £2 a week, that inflation is coming down, that interest rates are coming down and that the wide welcome for his statement on this side of the House will be reflected in manufacturing industry? The Government have recognised the important principle of the cost competitiveness of our industry.

Sir Geoffrey Howe: I am grateful to my hon. Friend, particularly for reminding me of the gap between the untruth that council house rents were likely to go up by £2 a week—I know not where that came from—and the reality of what I have told the House, which is that the increase in rents on which consultation will take place will be 85p a week, representing no real increase.

Mr. Shore: The Chancellor still has to answer the question that I put to him about competitiveness, and it is of great importance. What change, resulting from the national reduction in the national insurance surcharge, does he expect in Britain's international competitiveness and what will the figure be, bearing in mind that it was minus 36 immediately before he made his statement? We

[*Mr. Norman Fowler*]

the reduction in interest rates, the reduction now in the national insurance surcharge, are of profound importance for the development of social services in this country.

The Government's approach to social services has four main principles. First is our strategy to create the climate for industrial recovery. That is the foundation of our approach. It is only from the wealth that industry provides that the resources for the Welfare State can be created.

Second, we want to ensure that those most in need also benefit from the process of industrial recovery, while at the same time, we have done our utmost to protect those people during the present recession. Third, we are determined to secure better value for money by increasing efficiency and concentrating resources on care and treatment while also reducing the administrative bureaucracy by simplifying and streamlining procedures.

Finally, we want to see partnership between public and private in the areas of health and social services generally. We believe that it would be quite wrong for any Government to turn their back on the contribution that can be made, and is being made, by voluntary organisations in this country and also by the private sector. One of the most damaging and irrelevant policies of the Labour Party is its vendetta against the private sector. The aim should not be to destroy the private sector or to attack the voluntary organisations. The aim should be to try to harness every resource in our community to face not only what are the problems of today but what we should also recognise will be the continuing problems of tomorrow.

I wish to look first at the record of this Government and the facts of the position, not the generalised assertions. I start with health. In 1978-79 National Health Service expenditure in Great Britain was £7¾ billion. This year it is £14½ billion—almost double that amount. Expenditure has grown about 16 per cent. faster than the retail price index. Much of this extra money has gone into increased pay for staff and shorter working hours for nurses.

Resources for the Health Service itself have also grown substantially. I estimate that, with the fall in inflation this year, the scope for real growth in services to patients will be 5½ per cent. or more compared with 1978-79.

Mr. Alexander W. Lyon (York): The Secretary of State constantly makes this argument. Yet all those who go round our hospitals, as I did last week, see clearly that it is lack of financial resources that is squeezing staff and capital expenditure. Cannot the right hon. Gentleman see that, in a demand-led service like the Health Service, a mere 5 per cent. is actually cutting back on services because demand is growing at a far greater rate?

Mr. Fowler: The hon. Gentleman has made two points, first about growth and, secondly, about capital expenditure. On capital expenditure, it was his Government who presided over the biggest cut in such expenditure that the Health Service has known over the past decade. It was a cut of about 25 per cent. The hon. Gentleman was probably, I think, at that stage, still a member of the Government.

As for growth in the Health Service, the figures are those that I have set out. We have increased expenditure from £7¾ billion to £14½ billion at a time of the worst recession the world has known. I would have thought that Opposition Members would have found this pleasing. Self-evidently, that does not represent a cut in the Health Service. It represents a shift of priorities towards the Health Service in spite of the recession.

As a result, expenditure on health has increased as a proportion of GDP and it has also risen as a proportion of public expenditure, from 11·8 per cent. to 12·6 per cent. So, already, the figures show how absurd is the argument that we are seeking to cut the National Health Service.

Mr. Mike Thomas (Newcastle upon Tyne, East): Is it not the case nevertheless, that we still find situations arising in Great Ormond Street and elsewhere that should not arise——

Mr. William Hamilton (Fife, Central): And the Royal Marsden clinic.

Mr. Thomas: —I agree that the Royal Marsden breast screening clinic is another classic example. We still find, on the capital front, despite the Prime Minister's injunction to the Health Service last week, that health centres are not being built, orders are not being placed, wards are not being opened and capital construction is not being entered upon by regional health authorities. Such construction is frozen because the authorities cannot face the revenue consequences of the capital expenditure.

Mr. Fowler: The letter that we sent to health authorities made clear that what we planned was not a moratorium on capital spending. What we told them was that it was no use planning for capital spending unless they were sure of the revenue consequences that followed. It was designed to avoid the kind of situation that the hon. Gentleman has put forward.

With regard to Great Ormond Street, I have seen the chairman of the special health authority, and I hope that we shall have something further to say later this month when we have received the report on Great Ormond Street. The hon. Gentleman has been doing the social services job, if that is the job he is doing for the SDP, for long enough to understand that there will always be problems in the Health Service. That does not invalidate what I am saying, which is that the Government are devoting extra resources to the health services, not fewer.

Mrs. Elaine Kellett-Bowman (Lancaster): I am keen on Great Ormond Street hospital, having had a son whose life was saved there. However, does my right hon. Friend accept that those of us from the North-West are grateful to him and to his colleagues for redressing the wrongs of decades in hospital provision? In Lancaster we have a good hospital programme, and we are grateful that, for the first time, the under-resourced North-West is getting a fair crack of the whip.

Mr. Fowler: My hon. Friend makes the good point that, despite the recession, the Government have continued with the resource allocation working party policy, which I understand is supported by the Labour Party. We are trying to bring more resources to areas such as those represented by my hon. Friend, which have been under-resourced for many years.

Mrs. Gwyneth Dunwoody (Crewe): Will the right hon. Gentleman confirm that Merseyside, which is one of the areas of greatest need, will have a deficit next year?

are glad to hear that he is not engaged in warfare against the unemployed, but the best demonstration that he could give of that assertion is a clear and unequivocal pledge to restore the 5 per cent. that was taken away from the unemployed two years ago. It will not do for the right hon. and learned Gentleman to say that the Government have not thought about it and that it is inappropriate to give an answer. He has just made a statement about the uprating of pensions. Why cannot he do the same for the unemployed?

Sir Geoffrey Howe: I have said nothing about the uprating of pensions. I have told the right hon. Gentleman and the House that decisions about that will be announced at the time of my Budget.

In relation to the other matter about which the right hon. Gentleman asks, I shall go over the figures again. The changes in the national insurance contribution, the national insurance surcharge rates and the earnings limits that I have announced will save all employers £686 million in 1983-84, £450 million for the private sector, taking account of the effect of the rise in earnings between the two years. For all employers, after taking account of the reduction in contracted-out rebate announced in March this year, the total payments would have been about £12·8 billion. They will now be £12·1 billion. That represents a reduction of 5½ per cent. and therefore makes a significant contribution to the competitiveness of British industry. I reiterate that nothing can make as large a contribution to competitiveness as further success in achieving pay moderation. One day I hope to get that proposition endorsed by the Opposition.

Orders of the Day

Debate on the Address

[FOURTH DAY]

Order read for resuming adjourned debate on Question [3 November],

That an humble Address be presented to Her Majesty, as follows:

Most Gracious Sovereign,

We, Your Majesty's most dutiful and loyal subjects, the Commons of the United Kingdom of Great Britain and Northern Ireland in Parliament assembled, beg leave to offer our humble thanks to Your Majesty for the Gracious Speech which Your Majesty has addressed to both Houses of Parliament—*[Sir John Eden.]*.

Question again proposed.

Welfare State

4.20 pm

The Secretary of State for Social Services (Mr. Norman Fowler): I welcome the opportunity of this debate to set out again what the Government are doing in the fields of health, personal social services and social security, and to repeat our commitment to the development of the social service system, in particular the National Health Service. That commitment we have fulfilled and will continue to fulfil.

I should like first, however, to put the debate into context. That context as been provided earlier today in the statement by my right hon. and learned Friend, the Chancellor of the Exchequer. His announcement of the Government's decisions on next year's public spending plans demonstrated the essential connection between economic policy and the development of our social services. It is simply no good the Opposition declaring, as appears to be their policy, that they would increase spending on health and social security by anything between £10 billion and £20 billion. That would have intolerable implications for taxation, inflation and for the economy as a whole.

The social services and the Welfare State cannot be ring-fenced from the rest of the economy. Steadily improving services can be sustained only by steady improvements in industrial performance and competitiveness. In other words, to abandon the fight against inflation would hit first those who are most in need, particularly those on low and fixed incomes.

That is why the Government's achievement of the lowest inflation rate for over 10 years has important social implications as well. Between 1974 and 1979 prices rose in this country by 110 per cent. This Government have now brought inflation down to around 7 per cent. and the prospect is that over the coming months inflation will drop even further. That is vital to industry and therefore to social services policy generally because it is only with industrial recovery tha we can look ahead to developing social services.

It is for the same reason—that of helping industry and thereby the wealth-creating process—that the Chancellor's announcement of the reduction in the national insurance surcharge is also so welcome. The reduction in inflation, Econ Pol 2

Prime Minister 6

SECRET

DEPARTMENT OF EDUCATION AND SCIENCE

ELIZABETH HOUSE, YORK ROAD, LONDON SE1 7PH

TELEPHONE 01-928 9222

FROM THE SECRETARY OF STATE

5 November 1982

R Butler Esq
Principal Private Secretary
10 Downing Street
London SW1

Dear Robin,

On 2 November the Cabinet invited my Secretary of State to discuss urgently with the Chief Secretary how the package on student grants and "new blood" in 1983-84 was to be financed (CC(82)46th Conclusions, Minute 2).

2 The Secretary of State, who is out of London today, has asked me to let you know that he has agreed the following with the Chief Secretary. The Cabinet's decisions on student grants (no change in the minimum maintenance award, indexing of the parental contribution scale, some savings on travel expenses and an increase of 4% in the basic grant) will yield net savings of £3.2m, £6.8m less than the cost of the "new blood" programme in universities. The Chief Secretary has agreed to add half this sum, £3.4m, to the education and science programme and the Secretary of State will find the other half from savings elsewhere in his programme.

3 The Secretary of State is answering a Written Question on Monday about expenditure on education and science next year. The relevant passages on student grants and "new blood" read:

> "In the autumn of 1983, the main rates of grant will be increased by 4% and the parental contribution scale will be adjusted upwards by 8% in line with earnings in the past year, thus limiting the increase in cash contributions from individual parents. Revised arrangements will be introduced for meeting students' additional travelling costs, which will no longer be paid on the basis of separate specific claims.
>
> A separate announcement will be made about an additional allocation of some £10m which is to be made available to allow for a start in the autumn of 1983 on a programme

of recruitment by the universities of additional young researchers and lecturers, as well as for the provision of courses in new technologies primarily to improve the supply of qualified manpower in information technology. Part of this sum will be allocated by the Research Councils."

4 I am sending copies of this letter to the Private Secretaries to other members of the Cabinet and to Sir Robert Armstrong.

Yours ever,

Imogen Wilde

MRS I WILDE
Private Secretary

Econ Pol Public Exp Pt 17

5 NOV 1982

4

Ref. A09941

PRIME MINISTER

Public Expenditure Survey 1982:
(C(82)38)

BACKGROUND

At its meeting on 15th July, the Cabinet agreed that the aim in this year's Public Expenditure Survey should be to hold to the planning totals for 1983-84 and 1984-85. The Chief Secretary, Treasury was invited to hold bilateral discussions with spending Ministers and to report the outcome (CC(82)38th Conclusions, Minute 5).

Public Expenditure

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2. The memorandum by the Chief Secretary (C(82)38) carries out this remit. It reports success: the planning totals for 1983-84 and 1984-85 have been held. This is a considerable achievement, given the prospects in July. Bids (excluding consequences of the Falklands operation) totalling £6 billion in 1983-84 and nearly £8 billion in 1984-85 have been accommodated or withdrawn (which does make one wonder slightly about the justification for some of the bids in the first place). The decline since July in forecasts of inflation and interest rates has helped considerably; and bids totalling £2.5 billion in 1983-84 have been absorbed by reducing the contingency reserve for that year from £4 billion to £1.5 billion.

3. In addition, a number of reductions have been agreed between the Chief Secretary and the Ministers directly concerned. Three of these may cause political difficulties. They are mentioned in the Chief Secretary's separate minute of 1st November:

(i) Encouraging local authorities to increase council house rents by an average of 85p a week (6 per cent). This would allow some increase (£300 million; 10 per cent) in capital expenditure on housing; but less than the increase (£375 million) that could have been afforded, within the same total, if the Secretary of State for the Environment had maintained his earlier intention to press for increases averaging £1.50 a week.

(ii) A proposal to abate by 2.5 per cent the uprating of social security benefits in November 1983 in order to recover the excess provision for inflation which will be made by the uprating in November 1982. This saves £250 million in 1983-84, and over £700 million in a full year. If inflation continues to decline, this could mean a very low uprating in 1983. For this reason and others, it may be hard to secure the necessary primary legislation. The Chief Secretary therefore proposes a number of social security improvements, described in the Annex to his minute.

(iii) Reductions in student grants saving (net) £10 million in 1983-84, with consequentials in later years. The main feature is abolition of the minimum maintenance award (£410) payable to those with parents earning over £20,000. The sums involved are small; but in last year's Public Expenditure Survey the Cabinet objected to reductions in student grants (admittedly on a significantly larger scale). A statutory instrument, subject to negative resolution procedure, is required.

4. The Chief Secretary seeks approval for the figures he is proposing, which include figures for the external financing limits of the nationalised industries (Annex B of C(82)38). The figures would, however, be subject to minor technical adjustment: for example, the effect of the decision to set a public service pay factor of 3.5 per cent for 1983-84 has not yet been allocated to programmes, but appears as an overall deduction of £120 million.

FLAG B

Civil Service Manpower

5. The Chief Secretary also seeks agreement to the proposals in Annex C on civil service numbers for 1st April 1984: again, these might be subject to technical adjustments. The total is within

FLAG C

the Government's target of 630,000. The Chief Secretary is not seeking decisions on later years at this stage (paragraph 5 of C(82)38 makes this clear).

End-year flexibility

6. You will recall that in July the Chief Secretary circulated a memorandum (C(82)29), with an accompanying note by officials, outlining a possible scheme of end-year flexibility whereby Departments would be able, within limits, to carry over unspent provision from one financial year to the next. You decided then that the matter should be discussed in October, when the Chief Secretary's report on his bilateral discussions was available. Some Ministers with sponsoring responsibilities suggested that there should be analogous arrangements for the nationalised industries. Again, it was agreed between them and Treasury Ministers that the matter should be discussed in the autumn.

FLAG D

FLAG E

7. I minuted you on this subject on 22nd October and you decided (Mr Butler's minute of the same date) that it should not be taken at the present meeting unless the Treasury had a positive proposal to make.

8. As you know, there is concern at the prospective undershoot of public expenditure provisions (and its consequences for the public sector borrowing requirement (PSBR)) in 1982-83. Steps are being taken to reduce it. The Chief Secretary considers that it would be perverse to introduce a scheme of end-year flexibility now, since Departments, being able to carry forward underspends, would have less incentive to spend their provision this year. He does not intend to raise the subject at the meeting. If other Ministers raise it, he will probably take the line that this is not the time to introduce a scheme of end-year flexibility, but that he will be willing to consider the case for one sympathetically in the 1983 Survey, i.e. to take effect at the end of 1983-84.

Economic Background

9. We understand that the Chancellor of the Exchequer does not intend to circulate any documents about the economic outlook as background to the Cabinet's consideration of public expenditure, but will offer an oral report. This will not refer to policy measures currently under consideration.

NIC and NIS

10. At present the Chancellor does not intend to refer to the proposals on the National Insurance Contribution (NIC) and Surcharge (NIS) which were set out in his minute to you of 27 October. These have been agreed with the Secretaries of State for Social Services and for Industry and approved by you. As an aide-memoire in case the matter is, after all, raised, the essential points on the rates of NIS are:

FLAG F

Until August 1982:	3.5 per cent	
August 1982 to April 1983:	now	proposed
	2 per cent	equivalent of 1.5 per cent (by special deductions on payments in February-April 1983)
April 1983 onwards:	2.5 per cent	1.5 per cent

Announcements

11. If the Cabinet endorses the Chief Secretary's proposals on public expenditure, the figures for 1983-84 will be incorporated in the autumn Statement which the Chancellor of the Exchequer currently intends to make on Monday 8 November. (Figures for later years, and a detailed breakdown of the programme figures for 1983-84, will not be published until the public expenditure White Paper in the New Year.) He would amplify this in the economic section of the Debate on the Address; this might be supplemented by a short oral statement to Parliament, depending on the timing of Parliamentary events.

12. I understand that you have it in mind that you might make a brief reference to the outcome of the public expenditure exercise during the Debate on the Address on 3 November.

MAIN ISSUES

13. The main issues are as follows:

(i) Does the Cabinet endorse the Chancellor of the Exchequer's view of the economic background and the appropriate economic strategy?

(ii) Does it endorse the Chief Secretary's proposals on public expenditure (including the specific reductions mentioned in his minute of 1 November?

FLAG 9

(iii) (If the matter is raised), does it accept the Chief Secretary's views on end-year flexibility?

(iv) How and when should the Government's decisions be announced?

Economic Background

14. The Chancellor of the Exchequer will presumably point out that the outlook on both inflation and interest rates is better than when he reported to the Cabinet in July. He is likely to argue that this justifies the Government's economic strategy, and that it would be foolish to change it.

15. So far as we know, only the Secretary of State for the Environment is likely to challenge this assessment. He may well advance arguments similar to those which he deployed during the July discussion: that if the room for fiscal manoeuvre is used to reduce taxation, the benefits will be dissipated in higher pay, higher imports, or both; and that it would be better to increase public expenditure (particularly capital expenditure). Other colleagues may come in behind him, taking their cue from the pessimistic views of prospects now coming in from parts of British industry about the state of a "second round" of redundancies, and from the CBI Conference. You are familiar with this area of argument.

Public Expenditure: General

16. The outlook for public expenditure is more satisfactory than in July; and the Government will be able to claim credit for efficient management in sticking to the previously published figures. You will no doubt wish to congratulate the Chief Secretary on his success. But there are some potential weaknesses in the position for 1983-84 of which you should be aware:

(i) The Contingency Reserve

At £1.5 billion the contingency reserve for 1983-84 seems small: the reserve this year was £2.4 billion. True, it was sufficient to accommodate the short-term costs of the Falklands campaign. Against that, there are considerably larger uncertainties about the outlook for pay next year: the National Health Service dispute, in particular, has not yet been settled. Also relevant are:

(ii) The Nationalised Industries

The bids in July for additional finance in 1983-84 totalled £1.1 billion. The current proposals (which include the effect of the recent decisions on electricity prices) envisage no overall increase. But in 1980-81 and 1981-82 large increases had to be conceded; and there must be significant uncertainties about the prospects for industries such as steel, British Airways, and the railways.

(iii) Local Authorities

There are reports in the Press of a prospective overspend on local authority current expenditure in 1983-84 of some £1 billion (in addition to the £1.1 billion agreed in July).

Shortfall

17. On the other hand, as mentioned above, it seems likely that there will be substantial underspend on programmes in 1982-83. I understand from the Treasury that they expect a similar underspend in 1983-84. Some Ministers may argue that the figures for individual programmes should be increased to allow for this.

18. Against this, it can be argued:

(a) that the Government's expenditure planning already includes an allowance for likely shortfall;

(b) that other factors, such as those mentioned in paragraph 16 above, suggest that it could be difficult to hold to the planning totals in 1983-84;

(c) that it would be better to take a view of likely shortfall, and the implications for the PSBR, in the

New Year; the result can then be taken into account either in adjustments to expenditure plans or in the fiscal adjustment.

Public Expenditure: Specific Reductions

19. The Chief Secretary has agreed his proposals with spending Ministers; and all Ministers will see the force of the arguments for staying within the planning totals. There is unlikely to be much discussion of specific issues, with the possible exception of the three measures mentioned in the Chief Secretary's minute of 1 November.

Council Rents

20. It is not obvious why an increase in council rents averaging 6 per cent should be particularly contentious. (The Treasury do not want a larger increase because this would entail an increase in the social security programme to pay for higher Housing Benefit. This would not be fully offset in the housing programme, because the higher rents would, in part lead to higher surpluses in housing revenue accounts; these surpluses do not go to reduce public expenditure). But there may be issues on the timing of any announcement: there might, for example, be an adverse effect on the current dispute in the NHS.

Social Security

112

21. The uprating in November 1982 will increase benefits by 9 per cent - 2.5 per cent more than the forecast rate of inflation. There is an excellent case in logic for recovering the overshoot, as proposed, in November 1983. It will also save large sums of money. But the 1983 uprating could then look very small, especially if inflation is running at 5 per cent or less.

22. You will wish the Cabinet to reach a view on the merits of the proposal and how far it is necessary to go in offering concessions on the lines described by the Chief Secretary. The Chief Secretary can be expected to argue that if the Cabinet rejects any significant part of the savings he will have to reopen other programmes: he could hardly forgo over £700 million in a full year without effects elsewhere.

23. A particular point that may be raised by the Secretary of State for Social Services is the timing of any announcement. I understand that he is opposed to an early announcement. But it is hard to see how deferment could be helpful. The Government's position is likely to be easier if announcements are made as part of a series of decisions on public expenditure. There is the risk of leaks. And there is the further risk that the Government could find itself committed to whatever concessions may be agreed by the Cabinet, but unable to secure the savings.

Student Grants

24. The proposals on student grants include some items which, though small in terms of money, may hit some groups hard: in particular, it is proposed to abolish the minimum award, and this will mean that wealthier parents will pay more, perhaps considerably more. But the alternative is likely to be reduction in provision for university research and teaching in new technology ('new blood') which several Ministers believe to be important.

End-Year Flexibility

25. You will not wish to raise this issue yourself. If any other Minister raises it, the Chief Secretary can be expected to reply on the lines indicated in paragraph 8 above.

26. It is hard to quarrel with the argument that, given the prospective underspend in 1982-83, this would be a peculiarly bad time to introduce a scheme of end-year flexibility. It is equally hard to deny that the Treasury has consistently accepted the merits of a scheme but quarrelled with the timing; and that we should perhaps be in a rather better position now if we had introduced a scheme of flexibility in the past. Depending on the views expressed in any discussion you may wish to encourage the Chief Secretary to take a sympathetic view next year.

Announcements

27. There is no obvious reason to question what Treasury Ministers appear to have in mind on the timing of announcements. You will no doubt wish to remind your colleagues:

(a) of the need to avoid leaks;

(b) of the need to co-ordinate any more detailed announcements on their own programmes which they may wish to make.

HANDLING

28. You might open the discussion by inviting the Chancellor of the Exchequer to outline the economic background and prospects and the Chief Secretary, Treasury then to introduce his memorandum. Any of your colleagues may wish to speak; you will wish to encourage them to concentrate on points of principle or political significance; matters of detail should be resolved, if at all possible, between the Minister or Ministers concerned, and the Chief Secretary, Treasury.

CONCLUSIONS

29. You will wish the Cabinet to reach conclusions on the following:

(i) Does the Cabinet endorse, subject to technical revisions, the proposals in C(82) 38 on:

(a) the expenditure programmes (Annex A);

(b) the external financing limits for the nationalised industries (Annex B);

(c) the Civil Service manpower figures for 1 April 1984 (Annex C)?

(ii) Does the Cabinet endorse the specific measures discussed by the Chief Secretary in his minute of 1 November?

(iii) How should the Government's decisions be announced?

30. It may also be appropriate, depending on the discussion, to record the Cabinet's view of:

(iv) The Chancellor of the Exchequer's account of the economic background and prospects; and (if raised)

(v) A scheme of end-year flexibility in public expenditure;

(vi) The levels of NIS and NIC.

Lindsay Wilkinson

pp. ROBERT ARMSTRONG

1 November 1982

10 DOWNING STREET

Prime Minister

Robin

Message from Imogen Wilde re students grants:

- If you raise student grants by 4% rather than 5% the saving would be £5m.

- minimum maintenance award of £140 against present £410

Peter

Prime Minister 3

Mes 1/4

PRIME MINISTER

PUBLIC EXPENDITURE 1983/84: STUDENT GRANTS

A bad result of the squeeze on universities is that they cannot afford to recruit outstanding young people for scientific and technological research. I have had sober and sustained pressure from the research councils and universities about the damage that this will do to the quality of our work and therefore about the need to enable them to recruit some "new blood", as it has come to be called.

2 But within the relevant part of the education programme I have already had to use all the savings I can make to prevent an unintended worsening of the position in the universities and to keep the science budget as near stable in real terms as possible.

3 The only place I can look for further savings in order to mount a minimum "new blood" programme is student awards. It is for this purpose that I am proposing, as the Chief Secretary's minute of 1 November explained, to seek gross savings of £15m from the student award budget of nearly £800m.

4 Of the £15m of gross savings I would use £5m to raise the scale by which parental contributions are required - and this would be much welcomed by our supporters. The remaining £10m I would switch to "new blood".

5 In order to make the £15m savings I can either:

i Eliminate the minimum maintenance award of £410 paid to the 30,000 students whose parents earn more than about £20,000 a year; hold the increase in the main grant to 5% in line with the latest price increase forecast; and reduce the sum set aside for excess travel costs for students who live at some distance from their university or college.

4%.

OR:

ii Make a smaller reduction in the minimum award and cut the real value of the main grant for the third year running for 300,000 or 400,000 students.

6 I realise that the abolition - as opposed to the reduction - of the minimum award will be unwelcome to a small number of our supporters; but their children will continue to receive free tuition worth £10,000 or more for a three year course and they themselves have already benefited from our tax reductions - and may benefit further.

7 In my view, the first alternative is the better, both politically and educationally.

8 If the Cabinet approve my proposals I would expect to make an announcement about them very shortly after the Chancellor's general statement on our expenditure plans for next year.

9 I am sending copies of this minute to the other members of the Cabinet and to Sir Robert Armstrong. I shall be grateful if they will restrict its circulation in the same way as the Chief Secretary has asked us to handle his minute.

KJ

1 November 1982

G Prime Minister 2

Copy No. 1 of 30 Copies

Mus 1/11

CHIEF SECRETARY TO THE TREASURY

PRIME MINISTER

PUBLIC EXPENDITURE SURVEY 1982

I have circulated separately my proposals for public expenditure to 1985-86 following this year's Survey. They contain a small number of politically important items which you have agreed I should draw to colleagues' attention. Because of the sensitivity of these items, I know that you wish this minute to have a very restricted circulation. I therefore ask Cabinet colleagues not to circulate it outside their offices.

Local authority housing

2. The Secretary of State for the Environment and I have reached agreement on the net public expenditure for housing in a way which will allow gross capital expenditure to be increased by some 10 per cent (about £300 million) from the levels which seem likely to be achieved in 1982-83. On rents, the Secretary of State initially favoured an average increase of £1.50 (11%) but he now favours a rent increase of 6% - an average of 85p per dwelling per week. This will not affect the public expenditure total but the higher rent figure would have permitted a further increase of some £75 million in capital expenditure.

Social security

3. This year, as last, we are faced with the need for substantial increases in the baseline. Bids for extra demand-determined expenditure and other inescapable bids, taking account of the latest economic forecast, amounted to £815 million in 1983-84, £622 million in 1984-85 and £1200 million in 1985-86. There is, however, a difference from last year. The fall in the rate of inflation means that the uprating of benefits this November, which

was fixed at Budget time and based on the then expected inflation of 9 per cent, will be at least 2½ per cent in excess of the inflation now forecast for the year to November 1982. The Secretary of State for Social Services and I are agreed that we should recover this overshoot at the November 1983 uprating.

4. We established the principle of recovering overshoot by the action we took at the uprating in November 1981. We have made good a shortfall when that has arisen. Indeed, this year's uprating will actually be 11%, for it will include on top of the 9 per cent an additional 2 per cent to make good the shortfall last year. It was never intended (nor would it be fair at a time of generally falling or stable real incomes) to create a ratchet effect, whereby beneficiaries could never do worse than the rate of inflation but will from time to time do better.

5. The sums involved are £250 million in 1983-84, £725 million in 1984-85 and £775 million in 1985-86. The Secretary of State and I are agreed that we should seek to recover these amounts, both to offset the increases in this programme and to reinforce our strategy on work incentives. Nevertheless, despite its basic fairness, a proposal of this kind could encounter difficulties in Parliament. It may not be easy to secure the necessary legislation. Partly for that reason, I agree with the Secretary of State that we should use some of the savings obtained from the recovery to make a number of worthwhile improvements in social security, which we could not otherwise afford.

6. The Secretary of State and I have agreed a package of such measures, set out in the Annex. The most important are restoration of the 5 per cent abatement of invalidity benefit, and a start in 1983 in phasing out the earnings rule for retirement pensioners, leading to complete abolition from November 1985. There is substantial pressure from our own backbenchers for these changes. The Secretary of State and I are agreed that these improvements cannot be made if the overshoot is not recovered.

Student grants

7. There is provision for the basic student grant to rise next autumn by 6 per cent. The Secretary of State for Education and Science proposes net savings of £10 million in 1983-84 (with consequential effects for later years), by eliminating the minimum maintenance award (currently £410) payable to those with parents earning over £20,000; by holding the increase in the value of the grant next year to 5 per cent; and by reducing the amount set aside for extra travel costs. The gross savings of £15 million in 1983-84 will enable parental contribution scales to be indexed in line with earnings, reversing for 1983-84 (but not for 1982-83) the 1981 Survey decision.

8. The Secretary of State has accepted that if these savings are not approved, he should make corresponding savings elsewhere, probably by giving up an agreed addition for extra research graduates and new courses in high technology areas, including information technology.

9. I am sending copies of this minute to members of the Cabinet for their personal information and to Sir Robert Armstrong.

L.B.

LEON BRITTAN
1 November 1982

ANNEX

PROPOSED SOCIAL SECURITY IMPROVEMENTS

		1983-84	1984-85	1985-86
(i)	restore 5% abatement of Invalidity Benefit	20	56	59
(ii)	remove invalidity trap (1)	7	16	17
(iii)	increase income disregards for Supplementary Benefit and Housing Benefit (2)	5	15	16
(iv)	increase capital disregard for Supplementary Benefit	3	10	11
(v)	increase earnings rate for retirement pensioners (3)	18	45	20
(vi)	other possible measures	18	51	51
		71	193	174

(1) Anomaly whereby person receiving invalidity benefit can never qualify for long term rate of supplementary benefit.

(2) From £4 to £5; for one parent families increase in range of earnings over which half are disregarded from £4-£20 to £5-£26; and extension of this one-parent concession to long term unemployed family men.

(3) To £94 per week, with a view to complete abolition from November 1985.

- 1 NOV 1982

JV

(2)

Prime Minister

To note X particularly.

The Chief Secretary and Mr Heseltine are, apparently agreed on 85p and their idea is to leave it until Cabinet to see if colleagues would wish to propose a higher increase.

MLS 25/10

CHIEF SECRETARY TO THE TREASURY

Treasury Chambers, Parliament Street, SW1P 3AG

Rt Hon Michael Heseltine MP
Secretary of State
Department of the Environment
2 Marsham Street
London SW1P 3EB

22 October 1982

MO

Dear Secretary of State

PUBLIC EXPENDITURE SURVEY : DOE PROGRAMMES

I understand that all the loose ends on housing have now been settled. I am writing, therefore, to confirm the agreements we reached in our bilaterals and which form the basis of the figures I will beputting to Cabinet.

On water and Other Environmental Services, the record of our bilateral on 30 September sets out the figures and the terms of our agreement. And I have written separately about the PSA.

On housing, the position is more complicated as the baseline figure has to be adjusted to take account of other factors including changes in interest rates and the level of expected surpluses. The precise baseline figures have still to be settled but the assumptions on which they are to be calculated are:

(i) that the baseline capital expenditure figure of £1786 million should be increased by £50 million to £1836 million.

(ii) that an additional allowance of £70 million should be made for management and maintenance expenditure which local authorities will incur in 1983-84; but no allowance should be made for the expenditure in the aggregate of central government housing subsidy, block grant, or local authority expenditure targets.

(iii) that provision for net capital receipts should be increased by £350 million to £1105 million.

Taken together with a figure of 85p for rent increases, these assumptions produce a baseline total of about £2800 million. Our officials are agreed that this figure is realistic although they recognise that the current expenditure element may change slightly when final calculations are made.

The figures for the later years also need to be settled quickly. I believe this is best left to our officials in the first instance.

I have seen, and we have discussed, your letter of 20 October. On rents, you agreed not to proceed with an announcement of any increase in advance of the announcement of other Survey decisions. I should add that there is no disagreement between us that your preference for an increase of .85p instead of £1.50 would not have any net public expenditure effect and I will report this to Cabinet in the context of my general report on public expenditure. As for capital receipts, I am, of course, willing to consider any fresh evidence but I must say frankly that I will find it very hard to accept that any further change should be made to the assumptions we agreed at the bilateral.

I am copying this letter to the Prime Minister, George Younger, Nicholas Edwards, John Biffen and Michael Jopling.

Yours sincerely

JGI. Greve

for LEON BRITTAN

[Approved by the Chief Secretary and signed in his absence]

ECON POL : Public Exp Pt 21

E

PA (dealt with in Mr Butler's minute of 22/10 to Sir Robt Armstrong) Mes 22/10

Ref. A09812

PRIME MINISTER

End-year Flexibility for Public Expenditure Programmes

8/7/82. Pt 19. In July the Chief Secretary, Treasury circulated a memorandum to the Cabinet (C(82)29) on end-year flexibility for departmental public expenditure programmes. You decided (Mr Scholar's letter of Pt 20 23rd July) that this would best be discussed in October: this was, of course, when the Chief Secretary's report on his bilateral discussions with spending Ministers was expected to be available.

2. The circulation of the memorandum prompted some Ministers with sponsoring responsibilities to suggest that there should be analogous arrangements for the nationalised industries. Again, it was agreed between them and Treasury Ministers that the matter should be discussed in the autumn.

3. We understand that until quite recently Treasury Ministers did not wish the subject of end-year flexibility to be added to the Cabinet agenda for 28th October, when, on present plans, public expenditure is to be discussed. However, they now take a different view; and I gather that the Chief Secretary intends shortly to send you a minute, copied to Cabinet colleagues, referring back to C(82)29 and reaffirming his view that a scheme such as it discusses cannot be afforded this year. He also considers that there is no need for additional measures on end-year flexibility for nationalised industries since existing arrangements make adequate provision. He would wish these views to be endorsed by the Cabinet at the same meeting as that of which the public expenditure decisions are taken.

4. End-year flexibility is a matter on which the views of Ministers are likely to be divided. The Secretary of State for Defence is among those who have pressed for it as a means of solving the problems of overspending. This year there would

be considerable advantage in having a degree of end-year flexibility available to help deal with the probable underspend; it is a little surprising that the Treasury do not take this point. As the Chief Secretary's proposal is likely to be contentious, to include it in the agenda for the public expenditure Cabinet would complicate what looks as if it could be a relatively smooth discussion of the public expenditure plans. On the other hand, both the past correspondence and logic point to dealing with it at the same time as public expenditure generally.

5. In practice, once the Cabinet has taken the current round of public expenditure decisions and they have been announced, the possibility of end-year flexibility as between 1982-83 and 1983-84 will be ruled out. If therefore the matter has not been dealt with along with the public expenditure decisions, as promised in the summer, the Ministers who favour end-year flexibility (notably the Secretary of State for Defence) may feel that they have been deceived. That consideration argues in favour of trying to get end-year flexibility out of the way at the same time as the public expenditure decisions, as the Chief Secretary now wishes.

RtA

ROBERT ARMSTRONG

22nd October 1982

ECONOMIC POLICY.

Management and Personnel Office
Whitehall London SW1A 2AZ
Telephone 01-273 / GTN 273 4400

Gerry Spence Esq
Cabinet Office
Central Policy Review Staff
70 Whitehall
London SW1A 2AS

14 October 1982

WR 15/10

Dear Gerry

Thank you for the briefing which you provided yesterday for the Lord Privy Seal in connection with Lord Wells-Pestell's Question about the CPRS report on long-term public expenditure. The Lord Privy Seal found it very useful. Many of the supplementary questions were on DHSS matters and the briefing was very good.

The Lord Privy Seal is also most grateful to Mr Bailey and Miss MacKay for their help at the lunch time oral briefing. For this she is also indebted to Mr Mountfield (HM Treasury).

Copies of this letter go to Willie Rickett (No 10), David Clark (DHSS), Imogen Wilde (DES), John Gieve (Chief Secretary's Office), Richard Mottram (Defence), and Richard Hatfield (Cabinet Office).

Yours sincerely

Douglas Board

D R H BOARD
Assistant Private Secretary

CONFIDENTIAL

Prime Minister 2

GR 13/10

CABINET OFFICE
Central Policy Review Staff
70 Whitehall, London SW1A 2AS Telephone 01-233 7765
From: John Sparrow

Qa 06089

13 October 1982

Douglas Board Esq
Lord Privy Seal's Office
Old Admiralty Building
Whitehall
S W 1

MS

Dear Douglas,

I enclose material for Lady Young's use in replying to tomorrow's question from Lord Wells-Pestell about the CPRS report.

The material in sections B-D of the supplementaries and background notes have been supplied by DHSS and DES and seen by the Treasury. Part of the material in section A has been prepared on the advice of the Treasury but they may have further comments on it.

Mr Bailey and Miss Mackay will be available to attend the oral briefing which you plan to arrange for lunchtime tomorrow.

I am sending copies to Willie Rickett (No 10), David Clark (DHSS), Imogen Wilde (DES), John Gieve (Chief Secretary's Office), Richard Mottram (Defence), and Richard Hatfield (Cabinet Office), who should pass any comments direct to your office.

In view of the sensitivity of this subject, I should be grateful if recipients of the enclosed material would restrict its distribution to a minimum.

Yours ever

Gerry Spence

G B Spence

Enc

CONFIDENTIAL

House of Lords

Parliamentary Question for Oral Answer on 14 October

Lord Wells Pestell (Labour)

To ask HMG whether they will publish the recent report of the CPRS on the future of the welfare state.

SUGGESTED ANSWER

I assume that the noble Lord is referring to an analysis undertaken by the Central Policy Review Staff of possible ways of restraining the growth of public expenditure in the longer term. This was a confidential analysis prepared for Ministers and will not be published.

NOTES FOR SUPPLEMENTARIES

A THE CPRS REPORT AND PUBLIC EXPENDITURE

1. Why not publish report in view of extensive leaks and press discussions?

Government agree that debate about the long term problems of the welfare state and public spending should not take place on the basis of leaks and press speculation. But this CPRS document would not provide an appropriate vehicle for a public debate. (This is because it was not a self-contained fully worked out report but simply a list of possible options.) Moreover to publish a confidential document because it had already been leaked would encourage more leaks.

2. Will the Government prepare a document for public discussion?

It is for my rt hon Friend the Chancellor of the Exchequer, in consultation with my rt hon Friend the Prime Minister, to decide whether to initiate a public debate on the problems of public expenditure in the longer term, and if so how this might be conducted.

3. General questions about contents of the report.

Since no further action is to be taken on the CPRS document, the question of what it recommended or discussed has no practical significance for Government policy. For the record, however, the report did not make policy recommendations. It discussed a number of possible options for restraining expenditure (as a basis for deciding whether further work should be done).

4.	Has CPRS report been shelved?/What action does Government plan to take on the report?	The CPRS document has not been discussed by Ministers and no discussion is planned. But the Government will continue to seek ways of restraining the growth of public spending.
5.	Chancellor of Exchequer's Weekend World interview (10 October) shied away from major cuts in spending programmes. Have these been dropped?	I understand my rt hon Friend made very clear the need to restrain the growth of public spending and over time to reduce public expenditure as a percentage of national output.
6.	Why is it necessary to reduce public spending? (Other countries spend more as a percentage of national output.)	The present level of taxation is oppressive on the great mass of working people. In order to foster economic growth it is important to get tax levels - and interest rates - down. The only way of doing this, while keeping a grip on inflation, is to reduce the share which public spending takes of national output.
7.	Government split about need to cut public spending?	There is no disagreement on the need to restrain public spending, nor on the need to provide an adequate minimum level of care and standards for those in our society who cannot fend for themselves.

NOTES FOR SUPPLEMENTARIES

B. NATIONAL HEALTH SERVICE

1. Did report suggest abolishing/ privatising NHS?	[As I have already made clear] the report made no recommendations and has no significance for Government policy.
2. Will the noble Lady confirm that the Government have no plans to abolish the NHS?	I can certainly confirm this. As my rt hon Friend the Prime Minister said to the Party Conference last week "the National Health Service is safe with us ... the principle that adequate health care should be provided for all, regardless of ability to pay, must be the foundation of any arrangements for financing the health service."
3. Will the noble Lady reaffirm the Government's commitment to the NHS?	Yes. We have shown our commitment to the NHS by planning an increase in services of 5% in real terms between 1978-79 and 1981-82, and further growth is planned for this year.
4. Why are the Government considering alternatives?	This Government, like any other responsible Government, have a duty to make sure that every penny is properly spent. We would be failing in our duty if we were not to look at other ways of financing health care to see if they offered any improvements on the present system. That is why the former Secretary of State for Social Services set up a study to look at methods of financing, drawing on the experience of other countries. But as the present Secretary of State said on 30 July in another place:

"The Government have no plans to change the present system of financing the National Health Service largely from taxation ....."

5. Is not the Government encouraging private provision by stealth?

We welcome the growth in private health insurance. But there is no contradiction between this and supporting the National Health Service. Private insurance brings in more money, helps to reduce waiting lists, and stimulate new treatments and techniques. Our full commitment to the NHS is demonstrated by our record.

NOTES FOR SUPPLEMENTARIES

C. SOCIAL SECURITY BENEFITS

1. Does the Government intend to de-index the uprating of social security benefits as suggested in the CPRS report?

[As I have already made clear, the report made no policy recommendations and its contents have no significance for Government policy.] So far as social security benefits are concerned, there has been no change in the Government's position. Our policy has been to maintain the value of retirement pensions and other related benefits and that we have done. Next month's uprating, which will add some £3 billion to the cost of social security benefits, will protect the value of all weekly benefits.

2. If there are no present plans to de-index the uprating of benefits will a future Conservative Government - if re-elected - make this change?

I emphasise that there are no plans to alter the present arrangements. As to the future, all I can say is that, whatever Government is in power, - [and I expect it to continue to be this one for some time to come] - it will be the country's ability to meet the cost of public expenditure programmes which will be the determining factor in deciding their size and scope.

3. Will the Government restore the 5 per cent abatement of unemployment benefit?

Our position on this has been made clear. We reviewed the possibility of restoring the abatement when the benefit was brought into tax in July but concluded that we could not afford to do so. The matter is being kept under review and I have nothing more to add.

/4. Will there be an "overshoot" on this year's uprating and do the Government intend to claw it back?

4. <u>Will there be an "overshoot" on this year's uprating and do the Government intend to claw it back?</u>	Next month's uprating of benefits is based on a 9 per cent forecast movement in prices between November 1981 and November 1982. In addition, an extra 2 per cent has been added to compensate for the shortfall in last November's uprating. Inflation has been falling faster than was forecast at the time of the Budget and it is likely that the outcome will be lower than the 9 per cent forecast. We will not know the extent for a couple of months yet. The November 1982 uprating will, of course, go ahead as planned. The 1983 uprating will be decided nearer the time. It will depend on the forecast movement in prices, which will be made around the time of next year's Budget, and whether the Government decides to take account of any overshoot this year. No decision on this has yet been taken. Consideration of the outcome of the prices forecast is normal every year.

NOTES FOR SUPPLEMENTARIES

D. HIGHER EDUCATION

1. Is the Government considering any scheme for charging for higher education?

We are not considering any specific scheme, but it is naturally sensible that we should continue to review whether higher education is being organised in the best possible way in terms of the aspirations of the student, the economic and social needs of the country, and the burden that higher education provision places on the taxpayer.

2. Wouldn't any system of charging for higher education be unfair on the less well off?

This would of course mainly depend on the extent to which assistance in the form of scholarships or loans was available. Higher education currently directly benefits its recipients at the expense of the taxpayers - many of whom will never earn as much as most of the graduates they are helping to educate.

3. Shouldn't opportunities for free higher education be expanded?

The Government has to consider priorities right across the spectrum of provision, including for example the balance of expenditure between full-time higher education and opportunities for further education and training for those who leave school early.

4. Is the Government committed to intorducing a loan scheme for student grants?

The Government has reached no decision on the introduction of a scheme but Ministers are currently considering ways in which a loans element might be incorporated into the financing of student maintenance.

BACKGROUND NOTES

1. Lord Wells Pestell's question refers to the CPRS Cabinet paper on long term public expenditure whose main contents were leaked to the press in September and which has prompted widespread speculation about the Government's plans for the future of the welfare state, notably the National Health Service. (A selection of the main press comments is attached at Annex 1). Lord Wells Pestell is a former Labour DHSS Minister and it seems possible that his questioning will concentrate on the implications for the NHS.

2. The existence of a report has been admitted. The suggested answer gives the minimum of information about the document necessary to dispel the impression that the CPRS presented the Government with recommendations on "the future of the welfare state". The refusal to publish the document is in line with the practice of successive Governments in declining to publish CPRS work which gives confidential advice to Ministers. (Some CPRS reports are published - see Annex 2).

3. Refusal to publish this document still seems appropriate, notwithstanding the argument (e.g. Guardian 12 October) that it would be better to publish it than to allow debate to proceed on the basis of press leaks and speculation. This point is dealt with in the notes for supplementaries (A1).

4. The notes for supplementaries and the remaining background notes are arranged in four sections:

A. The CPRS report and public expenditure in general.

B. The National Health Service.

C. Social security benefits.

D. Higher education.

5. A background note on the CPRS is at Annex 2.

BACKGROUND NOTE

A. THE CPRS REPORT AND PUBLIC EXPENDITURE IN GENERAL

1. The CPRS analysis was commissioned in July this year, at the request of the Chancellor of the Exchequer, to complement the report which Cabinet had commissioned in March from a Treasury-led group of officials, on the likely pattern of public expenditure over the next decade.

2. Both papers were intended to be discussed at Cabinet on 9 September. In the event, the CPRS paper was not discussed. The Economist article of 9 October (Annex 1) purports to give an account of the Cabinet's handling of the issue.

3. The Treasury paper outlined two scenarios for growth and public expenditure over the next decade. It concluded that on a pesimistic (but not unrealistic) scenario public expenditure would consume nearly 6 per cent more of GDP than in the Government's first year of office, while on a more favourable scenario public spending's share of GDP would be only slightly below the 1979-80 level. The Treasury paper identified four main programmes (health, social security, education and defence) as accounting for over 60 per cent of all spending. Against this background, the CPRS was asked to identify possibilities for making "major structural changes" affecting the larger programmes. The resulting CPRS paper identified a number of possible major options (defined as options offering savings at least £1 billion per annum) in these four main programmes, as well as some other approaches. The main options in the CPRS paper are reasonably accurately outlined in the side-lined portions of the Economist article of 18 September reproduced in Annex 1.

4. While a fair amount of the subsequent press comment was speculation, it is evident that the Economist at least has a very accurate and comprehensive knowledge of the contents of the CPRS paper while it is known that the Times has a full copy of the Treasury report. Government Ministers have not denied the existence of either report. There has been no formal statement on the status of the CPRS document or its contents. However, the fact that the report has been "shelved", has not been discussed and will not be discussed by Ministers has been made widely known both through unattributable briefing and through press comments attributed to the Chancellor of the Exchequer and the Chancellor of the Duchy. At the Conservative Party Conference at Brighton on 9 October the Prime Minister, without referring to the report or the press controversy, made clear the Government's continuing commitment to the National Health Service (see Section B of this note and notes for supplementaries).

5. There may be supplementary questions about the "Weekend World" television programme in which the Chancellor of the Exchequer participated on 10 October. In this programme Professor Alan Budd gave his own projections of public expenditure, which showed public expenditure increasing as a ratio to GDP throughout the 1980s. The programme then discussed ways in which large cuts in public spending might be made. (A transcript of this section of the programme is not yet available.) According to the Treasury, the basis of the

figures used in the programme do not tally exactly with officially accepted figures. There seems no need for the Minister to be drawn into discussion about the programme's public expenditure projections.

6. In the second half of the programme the Chancellor of the Exchequer stressed the Government's intention to secure a reduction in the percentage of GDP being taken by public expenditure. He refused to be drawn on individual options and the general flavour of the interview was to play down the idea of spectacular cuts. There was no direct reference to the CPRS report. In planning public expenditure he also advocated public debate on how reduced public spending could be brought about. He hinted at savings through privatisation (mentioning the sale of council houses as an example) and emphasised that savings of considerable significance could be achieved through the pursuit of greater efficiency, eg in the NHS.

BACKGROUND NOTE

B. NATIONAL HEALTH SERVICE

1. Health services are planned to increase by 5% in real terms between 1978-79 and 1981-82 (cash provision up from £6½ billion in 1978-79 to over £11 billion in 1981-82). Further growth planned in current year.

2. Prime Minister reaffirmed commitment to NHS in speech to Party Conference on Friday 8 October. She said:

> "We have a magnificent record on the NHS. Naturally we have a duty to make sure that every penny is properly spent. That is why we are setting up a team to examine the use of manpower in the NHS. Of course we welcome the growth of private health insurance. There is no contradiction between that and supporting the NHS. It brings in more money, helps to reduce waiting lists, and stimulates new treatments and techniques. But let me make one thing absolutely clear: the NHS is safe with us. As I said in the House of Commons on 1 December: 'the principle that adequate health care should be provided for all, regardless of ability to pay, must be the foundation of any arrangements for financing the health service'."

3. Patrick Jenkin, when Secretary of State for Social Services, set up a working party of officials with two private sector consultants to explore ways of financing health care. Working party reported to Ministers earlier this year. Norman Fowler announced Government's decision in PQ on 1 July:

> "Between 1978-79 and 1981-82 the Government provided for increases in National Health Service services of 5 per cent. There should be some further growth in services this year. The Government have no plans to

change the present system of financing the National Health Service largely from taxation, and will continue to review the scope for introducing more cost-consciousness and consumer choice and for increasing private provision which is already expanding."

4. Government have taken a number of steps to improve efficiency and accountability in National Health Service. Examples include: reorganisation of Health Service, introduction of annual reviews of Regions at high level, development of statistical indicators to assist in monitoring performance. Two recent developments: planned introduction of quarterly manpower returns from Regions; announcement of a small team, led by senior representative of private industry, to examine ways in which NHS uses manpower and to make recommendations.

BACKGROUND NOTE

C. SOCIAL SECURITY

1. The fact that the CPRS document discussed deindexation of pensions and social security benefits was picked up and discussed in several papers. At Brighton the Prime Minister pointed out that the Government had kept its pledge to protect pensions fully from inflation. But she gave no commitments as to the future. This line is reflected in the notes for supplementaries.

2. Question C4 in the notes for supplementaries (possible clawback of this year's uprating of benefits) may well come up, given the imminence of the uprating and the controversy which always surrounds the issue.

BACKGROUND NOTE

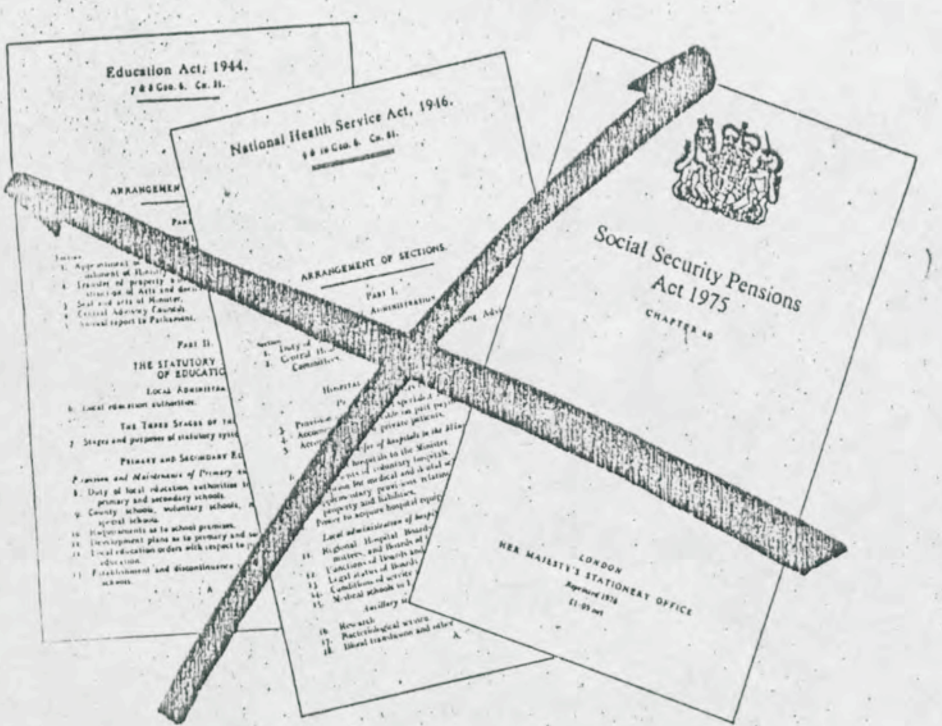
D. HIGHER EDUCATION

While publicity for the CPRS proposals was mostly focussed on the suggestion that there might be an increased measure of private financing for the health service, a scheme under which students would pay full cost fees for higher education courses, assisted in some cases by state scholarships, also received attention. A leader in The Times on 11 October discussed the possibility of charging and noted that some of the issues had been aired at the time of the Robbins report. The CPRS scheme is now shelved, but naturally ways of improving the organisation of higher education without increasing the burden on the taxpayer continue to be examined. The Secretary of State is particularly interested in exploring ways of encouraging diversity and fiscal independence in the university sector. DES is also currently discussing with the Treasury a scheme by which 50% of maintenance awards could be met by state financed loans. The details and timing of any such scheme have yet to be settled, and there is no Government commitment to its introduction.

ANNEX 1

PRESS REPORTS

THE ECONOMIST 18/24 Sept. 1982.



Thatcher's think-tank takes aim at the welfare state

The special meeting of Mrs Thatcher's cabinet on September 9th was devoted to a long discussion on the problems of controlling public spending. Far more intriguing, however, is what was not discussed: a paper from the Central Policy Review Staff, the government's think-tank, outlining options for radical cuts in public spending, many involving the dismantling of huge chunks of the welfare state. Cabinet wets were so appalled at the think-tank's suggestions that they argued successfully that it would be wrong for the cabinet to give it serious and instant consideration. But that will not be the end of the matter.

The think-tank's paper was circulated along with other cabinet papers on September 7th. It came with the seal of approval of the treasury, which recommended that it form the basis of a six-month study of a public spending strategy for the rest of the decade. This means that its ideas were not pulled out of the ether and that it has more significance than most think-tank papers. Here are details of its contents.

The paper begins by saying that, on present plans and assuming low annual economic growth, public spending will continue to gobble up at least its present 45% of gross domestic product for the foreseeable future. That is only 1% less than its peak under the last Labour government. If the Thatcher government is serious about cutting public expenditure, argues the paper, then it must consider some radical alternatives in the four areas that account for the lion's share of public expenditure: education, social security, health and defence.

The think-tank then deals with each one in turn:

- Education. Its most controversial suggestion is to end state funding for all institutions of higher education. Instead, fees would be set at market rates, at present around £12,000 for the average three-year course. About 300,000 state scholarships could be made available, along with student loans for those with the entry qualifications but without scholarships. The paper also says that there would be great savings if the state no longer had to provide for primary and secondary school education, but it acknowledges the political difficulties of abolishing state schooling. It considers moving to a system of educational vouchers for parents, which they could cash at schools of their choice to pay for their children's education. The idea has long been popular with free-market Tories and its supporters include Sir Keith Joseph (the education secretary) and Mr Ferdinand Mount (who recently became the head of the prime minister's policy unit in Downing Street). But the think-tank points out that vouchers would not cut spending and might even increase it, since parents at present footing the bill for their children's private education would qualify for state vouchers too. There are, however, some savings to be made in the school system by allowing the teacher-pupil ratio to rise. It has been falling, argues the paper, without any rise in the quality of state education.
- Social security. Big savings can be made, says the paper, if all social security payments—from pensions to supplementary benefits—no longer rise in line with inflation. There are echoes here of the Reagan administration's budget battles in the United States. The task of cutting federal spending in Washington has been made harder because of the political difficulties of abolishing the indexation of pensions.
- Health. The paper suggests replacing the national health service with private health insurance: this could save £3 billion-4 billion a year from a 1982-83 health budget of £10 billion. The problem is that the less well-off might underinsure, so the paper suggests that there might have to be a compulsory minimum of private insurance for everyone. In the meantime savings could be made by charging for visits to the doctor and more for drugs.
- Defence. The think-tank is short of bright ideas on how to curb the £14 billion now spent annually on the armed forces. It recognises that Mrs Thatcher does not want to budge from Britain's commitment to Nato to raise defence spending by 3% a year in real terms until 1986. It suggests, however, that beyond the mid 1980s defence's share of the nation's resources should be frozen. It points out that Britain spends a higher proportion of its gdp on defence than its

European allies and says that, in the long run, it would be to the country's advantage if defence was funded from the budget of the European community.

The think-tank's paper was circulated by Mr John Sparrow, the CPRS director and former merchant banker who is now widely regarded in Whitehall as a stalking horse for the treasury. A key drafter was Mr Alan Bailey (a treasury deputy secretary on loan to the CPRS, an expert on public spending and Mr Sparrow's deputy). In his own paper to the same cabinet meeting, Sir Geoffrey Howe, the chancellor of the exchequer said that a failure to shift social spending from its present trend would have severe consequences for the government's fiscal strategy. On the worst economic growth assumptions, and present welfare-state policies, the state's share of gdp could rise to almost 60% before 1990.

Treasury ministers were furious when the wets lined up en masse to block discussion of a paper which owed its inspiration to them. So was Mrs Thatcher. There is to be no record of the matter in cabinet minutes. The September 9th cabinet meeting produced the first wet-dry clash for over a year. It could be a harbinger of cabinet meetings to come. Mrs Thatcher sympathises with the think-tank's drift. But she is now in no doubt that to pursue such a radical course risks splitting her party wide open. Many of the think-tank's suggestions for health and education would be as unpopular with middle-class Tories as with Labour voters. But Tory wets expect that the think-tank's ideas will soon resurface in another guise.

Observer 19 September

Storm over secret Think Tank report

by AURIOL STEVENS

A FAMILY of four would have to pay £600 a year in health insurance and £950 a year for each child's school fees, if radical changes in public services, outlined by the Government's Think Tank were to be introduced.

It would also cost, on average, £12,000 to put a child through university, and all State benefits, including pensions, would be worth 10 per cent less than they are now.

The figures come from a discussion document circulated to members of the Cabinet this month by the Central Policy Review Staff. News of the document, which has been seen by THE OBSERVER, has caused a storm among both Conservative 'wets' and opposition politicians.

The report was drafted during the summer as a result of gloomy long-term economic forecasts drawn up by Treasury officials. Working on the most pessimistic projection for economic growth, the planning documents showed that maintaining public services at their present level would cost £12,000 million to £13,500 million more by 1990, an increase of around 10 per cent.

Since it is Government policy to reduce both borrowing and taxation, the Chancellor, Sir Geoffrey Howe, asked the Think Tank to devise ways of bridging the gap by cutting spending.

The report suggests that savings could be made by an 11 per cent across-the-board cut in all services. But this, it says, would be unpopular and impractical.

The Think Tank suggests instead a series of radical options, but warns throughout of the difficulties of carrying these through. The options are set out under three headings. The first, 'Partial Change,' suggests charging for higher education to save an estimated £1,000 million and increasing and extending charges for health services, to save another £1,000 million.

Under the second heading, 'Comprehensive Changes', they suggest charging for schooling, saving £3,000 million to £4,000 million; switching to a private insurance scheme in place of the National Health Service, saving £4,000 million; and de-indexing social security benefits, saving £3,000 million.

The third heading, 'Less Resources' suggests a cut of £1,000 million in education—and abandoning the present commitment to increase defence spending, to produce a saving of £1,500 million.

If the 'comprehensive changes' were introduced, the report warns, radical changes in the taxation and benefits system would be needed and these could be costly. 'If even the poorest had to pay full charges, this would exacerbate poverty to a level which we assume Ministers would judge unacceptable.'

It also warns that while public spending would be reduced, the proportion of 'the community's wealth' being spent on education and health would not be reduced.

Of all the options the two under the heading 'partial' are thought by Whitehall to be most feasible.

For higher education, savings of £1,000 million would be made if students were charged the full cost of courses. Means tested scholarships would be available for 300,000 students, or about three-fifths of the number of students now in higher education. Loans would be available for others.

Under health, the report says charges would have to be introduced for people now treated free — children and the elderly—for visits to GPs and for hospital places to produce savings of £1,000 million.

The Cabinet did not discuss the Think Tank's report in detail at the 9 September meeting, a meeting for which there are — exceptionally — no minutes. The departmental Ministers affected by the proposals have been asked to undertake further study of the suggestions and report back to the Cabinet.

Strenuous efforts have been made to prevent news of the exercise seeping out. When the first reports of it appeared in *The Times* two months ago, all copies of the relevant documents circulating in Whitehall were called in. Some members of the Cabinet are said to be anxious about the effects knowledge of such plans could have upon the party's electoral prospects.

HEALTH AND EFFICIENCY

The "Think Tank" to the right of them, the Labour Party Conference to the left: between the Scylla of a state-engineered takeover by private medicine and the Charybdis of a ban on private medicine altogether, what future for the National Health Service? The Central Policy Review Staff reportedly envisages up to a third of NHS activity being lured or pushed into the private sector: the Labour conference is committed to an annual rise of 3 per cent in its monopoly service's expenditure, regardless of the state of the national economy.

No future Labour Government could be bound by that commitment, of course. Meanwhile, the present Conservative cabinet is displaying in the most uninhibited way its own conflicts over the "Think Tank's" report. But the political options on either side do seem potentially more divergent than they have been for many years.

The travail within the Cabinet derives from a simple and grim piece of arithmetic (arithmetic being a factor wholly negligible to the Labour conference). Unless the whole economy grows at a rate of roughly $2\frac{1}{2}$ per cent (we should be so lucky), public expenditure will take a larger and larger share of gross domestic product, even after all the painful economies of the last three years. Without many fresh sacrifices, the promise to roll back state sector growth, will never be fulfilled.

The same dilemma involves social security, education, law enforcement, defence, and so on. Health spending has historically risen less fast than the first two, and the latter two are officially destined to rise faster than all the rest. The "Think Tank" report is said to make radical proposals in these other fields too. These deserve attention on their own account. But health is a particularly interesting case, because of the drastic changes proposed, and because the NHS is the principal embodiment in Britain of a particular ideal of social provision: the strong tang of ideology constantly attracts the flies of debate.

In addition, this week sees the publication of a notable addition to the debate, a public service contribution from the private sector a study of health provision across the world commissioned by the Nuffield Provincial Hospitals Trust. If pitched battle is joined over the future of the NHS, the study offers a salutary corrective to the prejudices of both sides. Its editors' eventual conclusion that the NHS "constitutes a unique and precious national asset" carries weight.

Not that anybody is proposing its abolition. There is no discredit to the Government in having commissioned a study of the theoretical policy alternatives, with no holds barred. But even the "Think Tank" envisages the survival of two thirds of the free service. All civilized nations, whatever their system of financing health, accept that a large proportion of the population cannot afford to pay for their own treatment. Today half the population are exempted from prescription charges, for instance, and they account for 60 per cent of NHS expenditure. Exemptions from an insurance-based system would have to be at least as wide. They represent a minimum obligation for any community to bear. The "Think Tank" reportedly proposes, perhaps only as an extreme case, a free service virtually confined to this category. The rest of the nation would negotiate for its health care with doctors and insurance agencies.

The arithmetic on which all this is based is not inexorable, but it is too threatening not to be frankly faced. At the outset, there is need for careful clarification of terms and objectives. There is an argument about public and private expenditure, and another about efficiency of service – related, but distinct. Endless muddle results from confusing the two. First of all, there is a presumption, generally well founded, that public expenditure is apt to rise at the expense of the productive investment (mostly private) which creates the growth that pays for all future investment.

The broad objective of restraining public sector growth to keep pace with the growth of the economy is a necessary and urgent one. It does not follow that the shifting of every service from public to private is equally helpful to that objective. Spending on health is not principally an earning activity whether it is in the public or private sector: it is a kind of investment in the national infrastructure, with some opportunity for invisible exports on the side. The case for a major shift into the private sector needs to show not only that it can be done without unacceptable harm to the disadvantaged, but also that it will facilitate the supply of care more effectively for a given cost to the whole economy.

Unfortunately, nobody has ever succeeded in defining wholly waterproof measures of effectiveness in health provision. There are too many outside factors, and too many subjective ones. There is no calculus for offsetting one pain removed here against another pain endured there. Much thought has gone into the defining of objectives in the NHS in recent years, and there have been advances, and consequential savings, though much more remains to be done.

The classic liberal case for transferring as much health care as possible into the private sector is that it enables the forces of the market to determine such priorities. The most significant contribution of the Nuffield study is to demonstrate how limited is the sense in which that is true. You cannot shop around intelligently for a kidney transplant. Insurance distorts the classical market, making the agency, not the patient, the effective customer. Monopoly distorts it even more – not the often-proclaimed "monopoly" of the NHS, which is a fiction till the Labour conference has its way, but the monopoly of skill and knowledge by the health professions used to protect themselves. Almost everywhere, the state is progressively moving into insurance-based systems to act as arbiter and planner.

If the objective of the "Think Tank" is to reduce overall spending on health, its proposals are either irrelevant or misconceived. The evidence from other developed countries is that the level of spending is related less to financial structure than to prosperity: legitimately, societies pay for as much in medical services as they can afford. There is also widespread evidence that with insurance-based systems costs, and particularly administrative costs, are not easier to control but more difficult. For all its defects, the NHS seems to provide a service at least as effective for the price as any other.

This is no consolation to ministers faced with that harsh arithmetic of growth and resources. The NHS is a system well fitted for hard times, and there are hard times to come. While the economy is marking time, subsidy to health must necessarily mark time too. Even if tax incentives could engineer the huge transfer of custom envisaged by the "Think Tank", the prospect of gains outweighing the administrative upheaval is remote. But private medicine does hold out the prospect of gains at the margin for the NHS, in response to demand. Private treatment can bring hospitals worthwhile income which can be applied to the benefit of all patients. The demand exists, and there is much to be gained by taking advantage of it by partnership with the private sector. The closer the partnership, the less the danger of that "two-tier" system which Labour's pay-bed policies did so much to foster in the 1970s.

In an imperfect world, the ideology of the market and that of unrationed free supply are equally unreal, and pursuing them is to pursue mirages.

"For forms of health supply let fools contest:
Whate'er is best administered is best"

Pope's formula begs many questions, but it points the way to empirical debates about ways and means – not easy, but productive – and away from fruitless controversies about a sterile and theoretical opposition.

Economist 9 October

1/24 Annex. Kag.

Mountains out of molehills?

The Thatcher government has botched its response to the think-tank report leaked to *The Economist*. It should publish the document as the start of a proper debate on the real dilemmas facing welfare spending in the 1980s.

The think-tank report, which suggested dismantling chunks of the welfare state, hung over the Tory conference like a dark cloud. In the run-up to Brighton, the prime minister's press office attempted what is known in Washington as a "damage-limitation exercise". The official line emerged that when Mrs Thatcher returned from her trip to the Far East she was so appalled by the reports that her government was seriously considering the think-tank's ideas that she immediately issued instructions for the report to be thrown into the rubbish bin. Since this involves a rewrite of recent history, it is worth reconstructing what really happened.

The think-tank report was circulated to ministers along with the rest of the cabinet papers on the evening of September 7th. The gist of its argument was that, on present spending plans and assuming low growth (½% to ¾% a year on gross domestic product), public spending would take 47% of gdp by 1990. That would be 6% above the share inherited by the Thatcher government in 1979.

The think-tank then outlined several options in health, education and social security for cutting the growth on public spending, so that the government could meet the 1979 manifesto pledge to reduce the share of the nation's resources controlled by the state. The most controversial suggestions were replacing the national health service with private health insurance (saving £4 billion a year); ending state financing of higher education except for 300,000 state scholarships; and limiting social security payments, including no longer raising pensions automatically in line with inflation (that could save £3 billion a year).

The think-tank report was circulated with an additional treasury recommendation that it might form the basis of six months' study of strategy on public spending. When Mrs Thatcher and Sir Robert Armstrong, the cabinet secretary, discussed the agenda for the special cabinet of September 9th, they decided to devote the morning to the more pressing problems of public spending for 1983-84 and discuss the think-tank report in the afternoon.

The day before that cabinet meeting, senior civil servants in each department briefed their ministers on what they might say about the paper. One minister said there were 18 civil servants at his briefing. On the eve of September 9th, several cabinet "wets" plotted how to kill the paper at the next day's cabinet.

Mrs Thatcher's first shock came before lunch during the cabinet meeting. She was surprised to discover that the think-tank paper had come with the usual cabinet papers. It should have been distributed separately to ministers only. It was feared that, as a result of its wide distribution within Whitehall, there was a strong chance of a leak. At least four cabinet ministers (all wets) said they did not want a formal cabinet discussion about its contents anyway.

When the cabinet broke for lunch, there was much intrigue. At one stage, Mrs Thatcher was closeted downstairs with treasury ministers, while upstairs the rest of the cabinet sat round the lunch table deciding how to kill the paper. When the cabinet reassembled, Mrs Thatcher was faced with a clear majority in favour of ditching the paper without further ado. Sir Geoffrey Howe and his chief secretary, Mr Leon Brittan, attempted a rearguard action to save the paper they had inspired. They were backed by Lord Cockfield, the trade minister, and Mr John Biffen, the leader of the house. Almost every other cabinet minister registered his disapproval. The prime minister expected the usual wets, such as Mr Jim Prior and Mr Peter Walker, to take fright. But more centrist figures (such as Mr Francis Pym) and respected veterans (like Lord Hailsham) were also opposed to considering it.

Mrs Thatcher argued that the cabinet should not shirk any paper that came before it. She was told by several of her colleagues that the think-tank exercise should have been done by the Tory party's own research department, so that there was less chance of it being branded as a indication of government policy. At this stage, Mr Cecil Parkinson, the party chairman, agreed that that might be the best way to proceed. In the end, an angry Mrs Thatcher bowed to the majority and ended the meeting without there being any discussion of the substance of the document. Next day the newspapers carried Downing Street lobby reports that the cabinet had simply considered public spending.

On September 17th, details of the think-tank paper appeared in *The Economist*. At Brighton, Mrs Thatcher was saying bitterly that it had been passed to us "within hours". In fact it took several days to leak out and was pieced together from a variety of sources.

Tory party managers were afraid that a think-tank controversy might overshadow a party conference which was supposed to celebrate the Falklands victory and the Tories' lead over Labour in the polls. Mrs Thatcher was aware of the troubles brewing at home while she was in Hongkong. On her return, she was told bluntly by Mr Parkinson that drastic steps had to be taken to dissociate the government from the think-tank's thoughts.

On Friday, October 1st, Downing Street briefed Sunday newspaper correspondents on Mrs Thatcher's supposed reaction to the think-tank. She was said to be against its report and had shelved it. Several Sunday and Monday papers carried a story along these lines, though some added their own caveats. In reality, Mrs Thatcher had shelved a report because she had met a cabinet brick wall.

The government's response to *The Economist's* original report should have been to publish the document as a basis for debate. There is a genuine quandary on how to finance welfare spending in the stagnant 1980s. In Brighton, Mrs Thatcher said she would not do that because the "think-tank language was too extreme". If so, she needs a more politically astute think-tank. If the report is to be shredded, then the government should mount a fresh exercise. It needs first a paper explaining how public spending will soak up more and more of the nation's resources in a low-growth Britain. A second paper should take a radical, but more comprehensive, look at public spending, embracing industrial as well as social policy. It is, as Mrs Thatcher herself says, absurd that these matters cannot be freely discussed. Why then is she trying to stifle them?

Thatcher's think-tank takes aim at the welfare state

The special meeting of Mrs Thatcher's cabinet on September 9th was devoted to a long discussion on the problems of controlling public spending. Far more intriguing ...

details of its contents.

The paper begins by saying that, on present plans and assuming low annual economic gro... spending will contin...

THE GUARDIAN FRIDAY OCTOBER 8 1982

Tackling the fiscal crisis of the welfare state

Peter Jenkins

THE "Think Tank" affair — more a chapter of accidents than a Thatcherite conspiracy to dismantle the Welfare State — has had the useful consequence of opening up a debate about the future of the public sector. At the same time it has opened the Government to a new line of attack from the "wets" whose buzz word this week has been "compassion." It has also illustrated the Prime Minister's remarkable capacity to be as resolute in retreat as she is in advance.

What happened was this. The Treasury about a year ago came to the conclusion that the dismal international outlook boded ill for domestic economic growth in the eighties. It made an internal analysis based on two rough and ready assumptions: the first (optimistic) took a growth rate around the average for the late sixties and early seventies; the second (pessimistic) projected the recent poor performance of the economy.

On the first assumption there would be a tricky problem in financing public expenditure; on the second the problem became horrendous. According to the leak in the Economist, public expenditure — on the worst assumption — could rise from 45 per cent of GDP to 60 per cent by the end of the decade.

The Treasury's assessment was passed to the "Think Tank" for comment. One of the functions of the "Think Tank" is to point up the wider policy implications of possible lines of action. What it pointed up in this case was that there was no way of balancing the books without radical policy change. In practice that meant radical change within the big four spending areas — health, social security, education and defence.

The "Think Tank's" thinking of the unthinkable was leaked by an outraged "wet." The Prime Minister returned from the Far East to find she had an embarrassing row on her hands. She went swiftly into retreat and repudiated the "Think Tank" paper.

The Treasury's analysis remains on the table, and the problem it exposes remains to be tackled by whoever forms the next government. One effect of the attention focused on the "Think Tank's" ruminations has been to obscure the Government's concern about defence expenditure which is at least as great as its worry about financing the NHS. Ministers are being taken to the cleaners by the Joint Chiefs of Staff who are taking ruthless advantage of the "Falklands Factor."

They have put in a huge bill — both for capturing and for the future defence of the Falklands — which they want settled over and above the defence budget. In addition they are demanding the indexation of the standard defence budget on the most generous terms plus the right to carry forward the huge sums which each year they are unable to spend.

The slogan of this Conservative Party conference is "The Resolute Approach." It is going to be intriguing to see how resolute the Prime Minister will be against the overweening military.

There are three courses this government, or any government, can take in trying to tackle what is becoming a fiscal crisis of the Welfare State. It can try to find the elixir of faster growth, in time to pay the bills. It can make radical alterations to the edifice of the post-war Welfare State. Or it can simply do the best it can in difficult circumstances, which would mean a good deal of privatisation and charging while the total of public expenditure as a proportion of GDP rose nevertheless.

This last approach was presumably what Mr James Prior had in mind yesterday when he joined in the argument and said: "We should not be too surprised or panic-stricken if, in the depths of recession, high unemployment pushes up the cost of a compassionate social policy."

The Prime Minister and the Treasury are unlikely to take so relaxed a view of the matter; nevertheless, ministers are already conceding that piecemeal measures—the privatisation of hospital cleaning, increase in health and educational charges for those who can afford to pay, and so on—are not going to take the measure of the problem if it presents itself on the scale envisaged on the Treasury's more gloomy assumption.

Even on that basis the arguments will be fierce. The "Think Tank" leak has given Mr Edward Heath, Sir Ian Gilmour and other dissidents the chance to accuse the Thatcher government of neglecting its social responsibilities, thereby departing from the true Tory tradition.

The accusation has some sting because the party managers know well from the opinion polls that a reputation for unconcern is the Prime Minister's weakest suit. Resolute she may be, and bold too, but does her Government have to be quite so bloody? Beyond the electoral considerations, and the moral considerations too, it is pledged within two terms of office to push back the frontiers of the state.

But those frontiers are defended by determined forces of vested interest, the public employees whose power and patronage has grown so in the last decade or so. They have in large part succeeded in hitching the Labour Party and trade union movement to their sectional cause.

The public v. private issue, which this Conservative Party conference has brought to the fore, is one which cuts across the lines of class and traditional allegiance to pare the public sector. It looks as if it will be the chief battleground of British politics in the years to come.

SINKING THE UNTHINKABLE

AT BRIGHTON

Beneath the placid surface of last week's Tory conference, a genuine doctrinal battle was being fought out over the future of the Welfare State. ADAM RAPHAEL and SIMON HOGGART assess the significance of a debate that began with a defeat for Mrs Thatcher in the Cabinet room at No. 10 last month.

OBSERVER

Sunday 10 - October 1982

THE CONSERVATIVE Conference chairman, Donald Walters, remarked plaintively at lunch one day: 'We try to get people to dissent, but nobody seems to want to.' The fact is that all Tory conferences are ruthlessly stage-managed. Motions are specially selected so that virtually every single delegate can agree with the wording. Speakers have to apply on a printed slip for their place at the lectern, so that they can be vetted by the platform first. As an official from the Soviet Embassy remarked with a smile in the tearoom last week, 'This is just how we organise *our* conferences.'

Beneath this glossy surface, however, the chasm which exists between the two different wings of the Tory Party gaped wider than ever. This time the wets believed that they were defending the whole concept of their Tory 'One Nation.' Mrs Thatcher tried to douse fears of a threat to the National Health Service in her conference speech, but by then the damage was done. The noise of battle over the future of the Welfare State echoed all round Brighton.

Mrs Thatcher can take some of the blame for this herself. She was warned by one of her closest allies: 'If we have got to think the unthinkable, for goodness' sake let us do it in private.'

In the interval between the anodyne debates in the conference hall itself, a parade of Tory wets, speaking in pubs and the private rooms of expensive hotels, launched their counter-attack on Thatcherism. They included Cabinet members such as Peter Walker and Jim Prior and members of the Government-in-exile, such as Ted Heath and Sir Ian Gilmour.

One Minister spoke privately of a 'monumental cock-up'; another talked bitterly about 'a botched attempt to dismantle the Welfare State.' Considering that the row is now likely to haunt the Tory Party right up to the next general election, it began quietly and innocently enough.

The Chancellor, Sir Geoffrey Howe, backed by the Prime Minister, decided that the Cabinet ought to have a wide-ranging discussion about the implications of accelerating growth in public expenditure, in an economy which was not expected to expand by more than 5 per cent over the next decade. The consequences would not seem just unpleasant —they would be disastrous. If nothing was done, according to a paper the Chancellor presented to the Cabinet on 9 September, the basic rate of tax would have to rise by half from 30p to 45p, and VAT would have to go up to 25 per cent.

Sir Geoffrey himself began the debate on the future of the Welfare State during the summer when he made a heavily coded speech in Cambridge. In it he set out the priorities for a future Conservative Government, and suggested that radical options would have to be examined if the Tories were to make good the pledge in their 1979 manifesto to reduce the share of the nation's income taken by public spending.

But it was not until Ministers received their Cabinet papers on 7 September, two days before the crucial meeting, that most of them realised that the Chancellor was now determined to force a swift examination of truly radical cuts in public spending.

In their official red boxes that evening, Ministers found three papers, one from the Chancellor, one from the Central Policy Review Staff, commonly called the Think Tank, and one from the Treasury on current public expenditure trends. All three made distinctly unpleasant reading. Sir Geoffrey's paper reinforced his threats of sharp tax increases by warning that public spending was set to grow to 47 per cent of Britain's gross domestic product by the end of the decade, much higher than when the Tories came into office. The consequences, he warned, were 'unacceptable and crippling disincentives to individuals and industry.'

The Chancellor's gloomy paper was complemented by the one written by the Think Tank. This set out a series of options for radical cuts in the Welfare State. Among its most controversial recommendations — which would save a total of £10 billion—were the introduction of compulsory private health insurance to replace the National Health Service, ending virtually all state funding of higher education, and going back on the Tory commitment to increase Social Security payments, including pensions, in line with inflation.

'I couldn't believe my eyes when this absurd paper came round,' said one Minister, a well-known wet. Another claimed he hadn't even bothered to read it, as it was so obviously 'a waste of time and energy.' Other Ministers, however, were carefully briefed by their officials on the options which the Think Tank had outlined.

The wets deny that they plotted together in advance of the 9 September Cabinet, but when the Prime Minister called the meeting to order that morning they were clearly fully prepared.

As soon as the Prime Minister read out the proposed agenda, suggesting that the Cabinet should spend the morning discussing the Chancellor's paper and devote the afternoon to the Think Tank, there were immediate protests. The wets, led by Peter Walker, the Agriculture Minister, said that the Think Tank's proposals were presented in far too vague and dangerous a form for the Cabinet to discuss. Others warned that the paper had had wide distribution throughout Whitehall. This was because the paper had been marked 'confidential,' a lower classification than 'secret' and much lower than 'top secret.' When Mrs Thatcher heard this, she was furious and demanded an explanation from the Cabinet Secretary, Sir Robert Armstrong.

As the morning passed, the Prime Minister's humour was not lightened by several of her

Ministers saying that they thought the Chancellor's own paper was unduly pessimistic and lacked any vision. At one point she exploded when Michael Heseltine, who has been pleading the case for more expansion, said drily that he wished for once that the Treasury would address its tiny collective mind to the question of promoting growth rather than always bewailing the lack of growth.

When the Cabinet broke up for lunch, the Prime Minister and Chancellor could clearly see that they faced a tricky afternoon. According to one version, after a fairly tense lunch, the Cabinet broke into two [illegible], with Mrs Thatcher, Sir Geoffrey Howe and Leon Brittan retiring downstairs to concert their tactics against the wets. But when the Ministers reassembled round the Cabinet table, it was quickly evident that the Prime Minister and the Chancellor had once again lost the support of a majority of their colleagues. It was not just the wets, but also the 'greys' and even some of the drys who indicated they thought it both futile and dangerous to proceed with a discussion of the Think Tank report.

The Health Secretary, Norman Fowler, said that the Think Tank proposals on the NHS were neither helpful nor relevant when the Government had already committed itself against alternative systems of financing.

Mrs Thatcher argued just as strongly that the issues were too important to be shelved and that the Cabinet had to face the facts on public expenditure, however difficult and unpleasant they might be. But the sense of the Cabinet had been caught by the wets, whose leader, Peter Walker, argued that while it was right for the issues to be debated, it should not be on the basis of an obviously flimsy, inadequate and ill-prepared paper. The correct place to start such a sensitive examination was in the party's research department. Lord Hailsham, who has been known to leave Cabinet meetings singing 'Oh God our help in ages past,' was heard to mutter instead that the paper had been the most damaging single episode of the past three years.

The argument — the first important wet victory for more than a year — was carefully omitted from the Cabinet minutes. But Mrs Thatcher's fears that details of the Think Tank report would soon leak out were confirmed eight days later when the *Economist* published a detailed account.

By then the Prime Minister was in the Far East, but she read with mounting anger reports cabled to her of the bitter political controversy caused by the leak. On her return, she summoned a crisis meeting and was advised by her party chairman, Cecil Parkinson, to cut her losses and disown the Think Tank report as 'politically inept.' This delicate operation, which inevitably involved a certain amount of glossing over what had actually happened, went wrong. Too many people knew what had been said and too many people were outraged by what they saw as a flagrant attempt to rewrite history.

So, when the party conference opened in Brighton last week, the wets were in no mood for submission. They know they cannot afford a full-scale Cabinet conflict so close to an election. On the other hand, they are not prepared to go into the election with a manifesto committed to dismantling the Welfare State at a time of massive unemployment. As Jim Prior told the Tory Reform Group: 'We shall not deal with these daunting problems by adopting the over-simplifications of those who like to call themselves nineteenth-century liberals . . . for us to take up nineteenth-century liberalism would have about as much appeal to the voters and as little sense as taking up Marxism has for the Labour Party.'

The wets can publicly protest, but their position is not strong. Mrs Thatcher has entrusted the vital job of co-ordinating the manifesto to Sir Geoffrey Howe, who together with Cecil Parkinson is in charge of the party's policy groups. With the Falklands factor still helping her, and with her party 12 points ahead in the polls, Mrs Thatcher still holds almost all the levers of Tory power.

But the issues raised by the row over the Think Tank report will not just die away. Mrs Thatcher has now been placed in a position where she has been publicly forced to admit that her Government cannot keep its pledge at the last election: to sustain the Welfare State while cutting tax at all levels of income. In the run-up to the election, Ministers are certain to have a difficult job facing questioners who will want to know which bits of the Welfare State are to be dismantled in order to prevent taxes increasing. As the Chancellor himself admits, the dilemma of accelerating public expenditure in a no-growth economy will not go away. Neither will the argument, which now seems set to dog the Tory Party throughout this crucial pre-election year.

The Tories may try to keep the wraps on this debate. But even if the unthinkable has now become the unspeakable, the voters will want to know precisely what the Government intends to do.

12 OCTOBER 1982

12 THE GUARDIAN

Slicing a cake full of fallacies

"The intention must be," Sir Geoffrey Howe told Weekend World this Sunday, "to secure a reduction in the percentage of gross domestic product (national income) being taken by public expenditure. It is now at 45-46 per cent, depending on how you measure it." A certain logic follows from the Chancellor's commitment. Either the share of public spending in national income can be cut by increasing national income, or it might be cut by reducing spending. The first course he effectively ruled out by promising years of low growth. The second is difficult. Sir Geoffrey inherited an economy where public spending took only 41 per cent of national income, and his recession has succeeded in creating enough unemployment to drive that share up. For the future, he murmured gently about the hopes of improving the efficiency of the public sector, but the truth is that such savings would amount to relatively little. Sotto voce, Sir Geoffrey was once again confirming that the Cabinet's dries may have "shelved" the Think Tank's proposals for education and the health service but they have not yet disavowed them.

More's the pity, then, that this report, evidently regarded by Mrs Thatcher and her Treasury ministers with intense seriousness, should not be regarded as serious enough to merit publication. Not serious enough even to be released for the examination of the Treasury committee of the House of Commons. Not yet serious enough to withstand the sort of scrutiny which our fiscal experts would like to give it.

It is highly contentious to suggest, for example, that the continuation of current policies and low rates of growth might lead to an expansion of the share of public spending to 60 per cent of national income, with consequent increases in income tax rates. Constant tax rates should be enough to fund a constant real level of public services, unless the number of recipients of pensions or supplementary benefit increases. The former is in fact unlikely, on present demographic trends. The latter will only occur if the economy is run for the foreseeable future at such a low pressure of demand and output that unemployment continues to grow. It then becomes not a public spending problem, but a problem of misguided government policies. If the economy does grow fast enough to reduce unemployment, then it is true that public spending may still rise as a proportion of national income. But that is the political result, observable in every developed economy for three decades, of the fact that the demand for public services increases disproportionately with rising income. It is a consequence of prosperity, not an obstacle to it.

From its analysis of a non-problem, the Think Tank glides effortlessly to counterproductive solutions. Most of its ideas would in fact entail the same or worse services taking a larger share of the national cake. Take, for example, health care. A brutal free market in health care would certainly reduce spending, but it would also leave poor people without care and has therefore been ruled out. "Privatisation" means instead a compulsory insurance scheme. But why does it make any difference, if the service remains the same, whether it is funded from tax or from compulsory insurance? In practice, the burden on the individual would increase. The costs of collection of premiums would be greater than the costs of collecting tax which has to be collected anyway. The Government's control over health costs would vanish, to be replaced by a system where doctors effectively decide the level of service and where consumers, their payments spread in thousands of premiums, are powerless to resist a steady increase in charges.

The same argument does not apply to private funding of higher education. The cost per student of perhaps £12,000 for a three year course would simply prohibit able working class students from going to university, for fear that the indefinitely rising unemployment which the Think Tank seems to posit would deprive them of an opportunity to repay the loans. "Education vouchers" for secondary schools, however, would certainly increase public expenditure. They would be a direct subsidy to those parents currently paying school fees and presumably they would also require the expansion of popular state schools if any meaning was to be given to Sir Keith Joseph's promise of greater consumer choice. Nor would standards necessarily improve. More middle class parents would vote with their children's feet for the private system, leaving many state schools deprived of resources or pressures for improvement. Like compulsory health insurance, "education vouchers" would be a way of spending more money on worse services. Can that really be the apotheosis of Sir Geoffrey's vision?

ANNEX 2

The CPRS

1. The Central Policy Review Staff (CPRS) was founded in February 1971 as an advisory and analytical unit within the Cabinet Office, serving the Cabinet and the Prime Minister. Its primary functions are to provide collective briefing for the Cabinet and its Committees; to prepare longer term studies and reports; and to monitor the Government's central strategy.

2. The CPRS currently comprises 14 advisers and 6 senior staff (including the Head of the CPRS, Mr John Sparrow and the Cabinet Office Chief Scientist) and 17 support staff. All advisers and senior staff are on secondment, mostly for about 2 years: there are no permanent appointments. About half come from outside central government (e.g. industry, local government).

3. It is not normal practice to reveal details of the CPRS' activities. Most of its work takes the form of confidential advice to Ministers. Some of its reports are published, however, and some of its activities are public knowledge.

4. Since its inception in 1971 the CPRS has published 13 reports, none between 1971 and 1973, 10 between 1974 and 1978, and 3 since 1979. This reflects changes over time in the balance of work as between reports for publications and confidential advice to Ministers. The latter is now the principal activity.

13 OCT 1982

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PISE SW

ECONOMIC POLICY

10 DOWNING STREET

From the Private Secretary

SIR ROBERT ARMSTRONG

Follow-up to Cabinet's Discussion of Long-Term Public Expenditure

The Prime Minister has noted your minute of 7 October with its suggestions as to how to carry forward the longer term review of public expenditure programmes.

The Prime Minister agrees that no specific action should be taken at this stage about the potential areas of study which affect several Departments, and which might be considered centrally. She will, no doubt, wish to consider further, after this year's public expenditure survey is completed, by, say, late November, how to proceed with the main body of the review, in particular on the social security, health, education and defence programmes.

M. C. SCHOLAR

11 October, 1982

CONFIDENTIAL

WH 11/10

CABINET OFFICE

Central Policy Review Staff

70 Whitehall, London SW1A 2AS Telephone 01-233 7765

From: John Sparrow

Qa 06080

11 October 1982

David Clark Esq
Principal Private Secretary to the
Secretary of State for Social Services
Alexander Fleming House
S E 1

Dear David,

Parliamentary Question

The CPRS has been asked to take the lead in handling the following PQ which has been tabled for oral answer in the House of Lords on Thursday, 14 October:

"Lord Wells-Pestell

To ask HMG whether they will publish the recent report of the CPRS on the future of the welfare state."

The question refers of course to the CPRS paper on public expenditure options whose contents were widely leaked to the press.

The suggested answer will found on the established principle that CPRS advice to the Government is confidential and is not customarily published. However, we shall need to provide supplementary briefing on the main points of substance which have featured in the public debate about the 'report'. Two of these, notably the future of the NHS and the indexation of benefits, fall within your Department's responsibility and I should be grateful if you could supply us with contributions to notes for supplementaries and background notes.

I should be grateful if Imogen Wilde (to whom this letter is copied) could provide similar contributions covering the financing of higher education.

Contributions (which should be copied to the Treasury) should be sent to Eileen Mackay (233 6094) to reach here by midday on Tuesday, 12 October.

Copies of this letter also go, for information, to Willie Rickett (No 10), Richard Mottram (Defence), John Gieve (Chief Secretary's Office), and Richard Hatfield (Cabinet Office).

Yours ever

Gerry Spence

G B Spence

Econ Pol
File

CONFIDENTIAL

bc JV.

10 DOWNING STREET

From the Private Secretary 11 October 1982

PUBLIC EXPENDITURE SURVEY

The Prime Minister was grateful for the Chief Secretary's note of 5 October.

She endorses the approach he has been following in his recent discussions with colleagues, and will herself be taking meetings on defence and electricity prices during the coming week.

The Prime Minister notes the areas of possible political difficulty singled out by the Chief Secretary in his report on the agreements he has so far reached. She has commented that she is content with what has been agreed - so long as these decisions can be got through the House of Commons.

I am sending a copy of this letter to John Kerr (HM Treasury) and Richard Hatfield (Cabinet Office).

M. C. SCHOLAR

John Gieve, Esq.,
HM Treasury.

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10 DOWNING STREET

From the Private Secretary

SIR ROBERT ARMSTRONG

The Prime Minister saw over the weekend your minute of 7 October (Ref: A09678) about the public expenditure survey.

The Prime Minister agrees to the procedure set out in Paragraphs 5 and 6 of the minute; except that she believes that the proposal for the 1983 social security uprating needs to be added to those identified in Paragraph 6 as requiring specific endorsement by the Cabinet.

M. C. SCHOLAR

11 October, 1982

CONFIDENTIAL

Econ Pol
Pub Exp.

Prime Minister

Content with this approach?

MCS 8/10

Ref. A09679

PRIME MINISTER

Follow-Up to Cabinet's Discussion of Long-Term Public Expenditure

The conclusions of the Cabinet's discussion of long-term public expenditure on 9 September invited all Ministers with responsibility for public expenditure to review their programmes critically with a view to contributing to a substantial reduction in public expenditure in the longer term; to discuss their proposals with Treasury Ministers and other colleagues as appropriate; and to report (CC(82) 41st Conclusions, Minute 4). The intention was that any further work on long-term public expenditure should be under close political supervision by the spending Ministers concerned.

Part 20

2. I imagine that you will want to get decisions on this year's Public Expenditure Survey out of the way, and also let the dust settle on the controversy over the CPRS report, before taking any initiative to follow up the Cabinet's conclusions on 9 September. Assuming that this year's public expenditure round has been completed by late November, it would then be timely to see what could most usefully be done to ensure that spending Ministers are, while recognising the political sensitivity of the issues, examining critically their long-term programmes.

3. As you know, two-thirds of public expenditure is accounted for by four programmes (social security, health, education and defence) for which, apart from the territorial Ministers, three Ministers are responsible, the Secretaries of State for Social Services, Education and Science and Defence. The exercise will achieve little without a political will on the part of those Ministers. It would also be desirable that you, Treasury Ministers and the spending Ministers concerned with those programmes should be broadly agreed on the political framework within which any further studies should be carried out.

4. This suggests that the best way of proceeding might be in two stages, as follows:

(i) As soon as this year's Public Expenditure Survey is out of the way, you, together with the Chancellor of the Exchequer and the Chief Secretary (and perhaps the Home Secretary) might have a series of separate meetings with the Secretaries of State for Social Services, Education and Science and Defence to consider how the Cabinet's conclusions of 9 September might best be carried forward in their areas.

(ii) Assuming that a reasonable basis for progress can be established in those areas, you might then set the exercise in train generally with a minute to the Chancellor, copied to all members of the Cabinet drawing attention to the relevant Cabinet Conclusions on 9 September and asking that reports prepared in consultation with Treasury Ministers and other colleagues as appropriate should be sent to you by the beginning of March. The aim would be to discuss the reports between the Budget in mid-March and, say, end-April when next year's public expenditure exercise will be put in hand. You might wish at that stage to set up a small group of Ministers to consider the reports rather than have them put to the full Cabinet, but that decision could be deferred until we had a better idea of what the reports would be likely to look like.

5. In your summing up of the Cabinet's discussion on 9 September you said that there were also "potential areas of study which affected several Departments and might therefore better be conducted centrally" and that you "would give further consideration to how such studies might best be organised". I am assuming that you do not want to have any specific action taken about that at this stage.

No - I have
made several comments
on John Sparrow's minute.
MT

RtA

ROBERT ARMSTRONG

7 October 1982

Ref. A09678

Prime Minister (1)

Agree the proposal in paras 5 and 6, as amended?

MLS 8/10

Yes not

PRIME MINISTER

Public Expenditure Survey

Introduction

The minute of 5th TPM. October from the Chief Secretary, Treasury reports progress in carrying out the Cabinet's decision (CC(82)(38th 20) Conclusions, Minute 5) that the aim in the current public expenditure survey should be to hold to the planning totals in the 1982 Public Expenditure White Paper.

2. The figures for 1983-84 stand as follows:

		£ billion
Baseline:	programmes	116.3
	contingency reserve	4.0
		120.3
Net additions to programmes resulting from decisions to date		1.8

The prospective net addition to programmes can be met, in the Chief Secretary's view, by reducing the contingency reserve by £1.8 billion to a new total of £2.2 billion.

3. In addition, there are outstanding issues on programmes (mainly defence, including the Falklands Garrison) and the nationalised industries (mainly electricity supply) totalling about £2.1 billion. The Chief Secretary, Treasury proposes that defence and electricity should be the subject of meetings between yourself, Treasury Ministers, and the spending Ministers concerned. He also mentions a number of matters which have been agreed between himself and the spending Minister but which may be politically contentious: a reduction in the real value of student grants, and an increase of council house rents by an average of £1.50 a week.

General Position

4. The Chief Secretary proposes that the contingency reserve for 1983-84 should be £2.2 billion. He suggests (paragraph 9) that this might be further reduced by an unspecified amount in order to accommodate an increase in the defence programme. The result of that would be a reserve significantly less than this year's (£2.25 billion). This could be hard to hold. It is true that this year's reserve was adequate to accommodate the short-term costs of the Falklands campaign. Against this, the other pressures on the defence budget have been a good deal less than in some previous years; and central Government pay settlements next year may be harder to accommodate than they were this year (even now, there is the continuing uncertainty of the NHS pay dispute). There will be little room for manoeuvre if expenditure in 1983-84 is to be held to the planning total. This may affect the view of outstanding bids during the remaining part of the survey.

a. Defence

The figures are still fluid. There are no firm decisions - still less firm estimates of costs - regarding the future of the Falklands Garrison and the airfield , on both of which proposals are due to be taken by OD(FAF) in early November; and there is still dispute about the application of the pledge of 3 per cent real growth and the alleged relative increase in the prices of defence equipment. Treasury and Ministry of Defence officials hope to produce an agreed statement of the outstanding issues within the next few days. This will have to be settled between you, the Chancellor, the Defence Secretary and the Chief Secretary.

b. Electricity prices

The issues are described in the attachment to the Chief Secretary's minute. The electricity supply industry in England and Wales is bidding for an increase of up to £0.1 billion in its External Financing Limit for 1983-84. A price freeze would cost a further £0.5 billion. The Chief Secretary appears to accept that some reduction in price increases is justified, but does not indicate the likely cost. Decisions relating to England and Wales can be expected to have consequentials for Scotland.

c. Social Security uprating

The November 1982 uprating is based on a forecast of 9 per cent price inflation;

the latest forecast is $6\frac{1}{2}$ per cent. The Chief Secretary and the Secretary of State for Social Services have agreed to recover the excess of $2\frac{1}{2}$ per cent at the November 1983 uprating. But this could entail a very low uprating. Ministers collectively may see political difficulties in this. It may also be argued that to restore the 5 per cent abatement of unemployment benefit, which the Chief Secretary suggests would be among the concessions needed to make the low uprating acceptable, would have undesirable effects on the labour market.

d. Student awards

The details have yet to be worked out; but the Secretary of State for Education and Science has undertaken to find £10 million of savings in 1983-84. It is likely that he will do so by holding back increases in the level of awards to students living away from home. A proposal on these lines was part of the student grants package rejected by Cabinet last year. But the sums at stake are pretty small.

e. Council house rents

The Secretary of State for the Environment has agreed with the Chief Secretary on measures which are calculated to lead to increases in council rents in England averaging £1.50 a week (12 to 13 per cent); the intention is to release funds within the housing programme for more capital expenditure. The effect on the Retail Price Index would be relatively small. But it would be politically contentious; Ministers may particularly wish to consider the possible implications for the attitude of the mineworkers.

Procedure

5. The Chief Secretary's proposal for restricted meetings under your chairmanship to consider defence and electricity prices seems sensible. There would be little point in setting up a Ministerial Group under the Home Secretary's chairmanship, as we thought might be helpful at an earlier stage of the public expenditure exercise. If there is to be a meeting on electricity prices, it would probably

be right to include the Secretary of State for Scotland as well as the Ministers suggested by the Chief Secretary. It will be important to ensure that papers for any meetings that may be arranged are agreed between Departments so far as the facts are concerned and circulated in sufficient time beforehand.

and social security uprating MLS

6. The student grants and council house rents proposals should be specifically endorsed by Cabinet. There should be no need for special meetings on the other issues mentioned in the Chief Secretary's minute.

RA

ROBERT ARMSTRONG

7th October 1982

c/c JV

(1)

Prime Minister

Agree to take meetings on defence and electricity prices?

Yes

Content with the agreements reached so far – including on social security and education?

Yes if they work out get through the House not.

CHIEF SECRETARY TO THE TREASURY

PRIME MINISTER

PUBLIC EXPENDITURE SURVEY

At its meeting on ~~15~~ 1st July, the Cabinet agreed that our aim in this year's Survey should be to hold to the planning totals in the 1982 White Paper. I was invited to hold bilateral meetings with colleagues with a view to securing this objective.

2. I have now held discussions with all our colleagues who have responsibility for major programmes of expenditure. There are still a few loose ends - and some major difficulties - but, after some tough and extensive negotiations, we have made good progress and I believe we can come close to meeting the Cabinet's objective. In this minute I seek to inform you of the present position and to consult you on the best way to resolve the remaining problems.

3. The position so far is:-

	£ billion
(1) Baseline (after Budget changes)	120.3
(2) Bids at the time of the July Cabinet	
Local authority current (reduced from an initial £1.6 billion)	1.1
Programmes	4.0
Nationalised industries	1.1
Total	6.2

(This does not cover the bids for the Falklands Garrison or electricity prices which had of course not crystallised by then)

(3) Outcome of discussions to date:

Additional Local authority current		1.1
Net Additional expenditure on programmes		0.7
Revised economic assumptions (tentative estimate)		0.3
		2.1
Less: Further special sales of assets	0.2	
Clawback for $3\frac{1}{2}$ per cent pay factor	0.1	
	0.3	
		0.3
Addition to baseline		1.8

(4) Outstanding issues:

Programme bids unresolved (mainly Defence but excluding Falklands Garrison)	0.9
Falklands Garrison	0.5
Nationalised Industries	0.7

The nationalised industries figure following the bilaterals is now very close to the baseline, except for the major problem of the electricity EFL and electricity pricing proposals (see para 7b)

4. Thus, leaving aside the outstanding issues, the addition to the total allocated to programmes last year would be £1.8 billion. But the planning total in the 1982 White Paper includes a Contingency Reserve of £4 billion, a figure which was, of course, deliberately larger than we need for an operational reserve. Were there no outstanding issues, we could certainly hold to the White Paper total by reducing the Contingency Reserve by £1.8 billion leaving a reserve for the year of £2.2 billion.

5. To achieve this position, some decisions are assumed to which I should draw your attention. An important element of the

package would be the recovery of a $2\frac{1}{2}$ per cent overshoot in the 1982 social security uprating. This saving is worth about £250 million in 1983-84 and £750 million in a full year. There are obvious political difficulties about this, but Norman Fowler and I are agreed that it is the right course to take and that it can be made acceptable by certain other concessions. These would include restoration of the 5 per cent abatement of unemployment benefit and partial abolition of the earnings rule.

6. There are two other areas of possible political difficulty in the packages which I have so far agreed to recommend to Cabinet. Keith Joseph's offer of a saving of £10 million on student awards will involve a real reduction in student grants, which some colleagues may find it difficult to accept. On housing, Michael Heseltine and I have reached agreement on the public expenditure totals, but he will wish to seek Cabinet endorsement of his proposal to increase council house rents by an average of £1.50 a week.

7. There remain, then, a very limited number of outstanding but important difficulties:-

(a) On defence there are still a number of unresolved issues: the total bid, on which there is so far no agreement, is for an extra £1.3 billion (including the Falklands Garrison);

(b) the figure for the electricity supply industry is also not settled. There is a substantial bid to increase the industry's 'basic' EFL due to a number of pressures for increased expenditure or reduced revenue which the industry has been unable to offset by reducing costs elsewhere. In addition, there is a further bid for moderation of electricity prices over the years 1983-86 at a cost of £500 million or more a year (the details are summarised in the attached note);

(c) I have still to reach agreement with Francis Pym over bids of about £30 million and with David Howell and

Peter Walker over smaller amounts. Discussions of these bids are continuing and I am reasonably hopeful that we shall be able to reach agreement.

8. Our ability to adhere to the White Paper figures is, therefore, likely in the end to depend on our handling of the defence and electricity issues.

9. On defence, the problems undoubtedly remain difficult; but if we could settle on a modest increase to the programme provision and further adjust the Contingency Reserve, I am satisfied that our public expenditure aims could be met without impinging on the 3 per cent NATO commitment and without re-opening what has been agreed on handling the Falklands costs. I imagine that - as John Nott has suggested - you would yourself wish to chair a meeting on the defence programme, which Geoffrey Howe, John Nott and I would attend. I would naturally expand on these comments in a paper for that meeting.

10. This leaves the electricity supply industry - and its pricing policy - as probably the most awkward of our problems. The scale of the difficulty over pricing is such that it could make all the difference between our success and failure in meeting the Cabinet remit. On present plans electricity pricing is to be discussed in E next week, but I understand that Nigel Lawson is having some difficulty in obtaining the figures he needs from the industry. In any event, because of the importance of this issue to public expenditure, you may think it useful to have an early meeting on this with the Chancellor, Nigel Lawson and myself.

The Chief Secretary ~~[illegible]~~ has in mind a meeting before E, and even if the detailed figures are not yet available.

11. I would of course be happy to provide details of the provisional agreements which I have made with the majority of our colleagues, and any further information that you may require.

12. I am sending copies of this minute to Geoffrey Howe and to Sir Robert Armstrong only.

L.B.

LEON BRITTAN
5 October 1982

ELECTRICITY SUPPLY INDUSTRY (ENGLAND AND WALES)

The Secretary of State for Energy has indicated that he will be putting forward a substantial additional bid, above the White Paper baseline, totalling more than £½ billion for additional external finance in 1983-84 for the electricity supply industry in England and Wales (ESI).

2. The reasons for this bid are complex. One element is due to several pressures for increased expenditure or reduced revenues which the industry has been unable to offset fully by lower costs elsewhere.

3. The largest element in the additional bid is due to the Secretary of State's wish for price moderation, perhaps even a price freeze for the ESI in 1983-84. Every one per cent off electricity prices adds £70-£80 million to public expenditure. A price freeze compared to the assumption of a 7 per cent inflation rate in 1983-84 would cost some £500 - £550 million.

4. The Secretary of State's suggestion for price moderation next year follows a review of the industry's price structure by Coopers & Lybrand. It has been the policy since the 1960s to aim to set electricity prices equal to marginal costs (ie. to charge the customer for the consequences of a change in his demand for electricity). One element in these costs - representing about 20 per cent of them - has been the cost of the additional plant needed to meet an increase in demand. But because the industry will continue to have substantial over-capacity, it is not planning to build new power stations for the foreseeable future (other than nuclear stations which are justified on cost-saving rather than capacity grounds). Coopers' argument is that the plant element in marginal costs should reflect, not a new station, but the much lower cost of deferring the retirement of an existing station. The precise effect of this approach on marginal costs (and hence prices) has not yet been determined, but it is thought that they might be up to some 10 per cent lower in real terms than at present.

5. The Treasury accepts that Coopers' arguments point to <u>some</u>

moderation in electricity prices over the next few years. But the phasing of the moderation should depend on, besides the technical marginal cost arguments, the requirements of the Government's public expenditure/PSBR policies. The degree of price moderation sought by Mr Lawson should therefore be phased over a few years. In political terms too, the credibility of a once and for all change of the order proposed, based on a technical study of pricing policy, is questionable. It would seem to imply that for some time now we have allowed electricity prices to be far too high.

Beneficiaries

Why not - 'if' they have been overpaying'

6. The precise beneficiaries of the price moderation are still unclear. But since the intention is to moderate the general level of prices a large proportion of the benefits would probably go to domestic and commercial consumers (shops and offices etc) (roughly 60 per cent). The rest would go to industry. The intensive electricity users would benefit proportionately least. They already receive many of the benefits of the arrangements recommended by Coopers through the scheme announced in the last Budget.

-5 OCT 1982

Econ Pol

Hall (HMT)
Gieve HMT
Kerr HMT

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Draft prepared by PM + Sir R Armstrong sent to Treasury. MCS 1/10

DRAFT PRESS NOTICE

PUBLIC EXPENDITURE PLANNING AND PAY

As is usual at this time of year the Government is reviewing its plans for public expenditure. As part of the process of reaching final decisions on the cash total for each programme for 1983-84, it is necessary to decide what provision should be made for wages and salaries. Such provision is determined principally by the numbers employed and the rates at which they are paid.

A decision has now been taken to budget for sufficient additional cash in 1983/84 to provide for average increases in wage and salaries bills by 3½% from due settlement dates.

This decision concerns the cash provision to be made in public expenditure. It is not a pay norm. Each Department has its own specific budget, within which expenditure on wages and salaries must be accommodated.

This decision relates to those groups for which provision is made in monies voted by Parliament, save that a decision about the provision for the wage and salaries element in health service expenditure is not being taken for the present. It does not directly cover the local authorities or the nationalised industries,

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/ which

which are not within the Government's direct control, but they will be constrained respectively by the rate support grant proposal and by External Financing Limits.

NOTE FOR EDITORS

A similar announcement about the provision for pay in 1982/83 was made on 15 September last year. The rate of inflation is already much lower than at this time last year, when the corresponding figure for 1982/83 was fixed at 4%.

1.10.82

PART 20 ends:-

28.9.82

PART 21 begins:-

1.10.82

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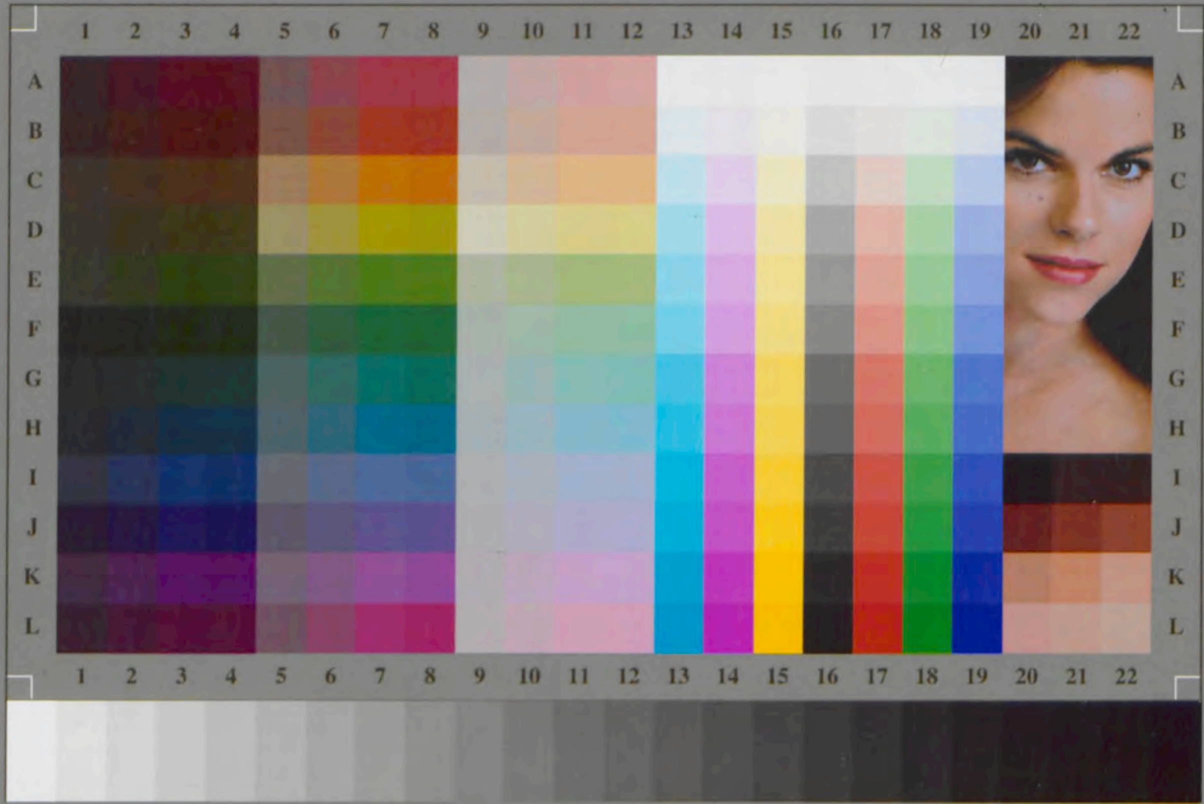

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