

1. Summary and timetable of urgent economic issues.
2. The Budget.
3. Public Sector Pay and Cash Limits.
4. Energy.
5. European issues (including the EEC Budget and CAP).
6. House of Commons Procedure: Open Government:
Official Secrets.
7. Devolution.
8. Northern Ireland.
9. East/West Relations.
10. Comprehensive Test Ban Negotiations.
11. SALT.
12. Rhodesia.

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PRIME MINISTER

Summary and Timetable of Urgent Economic Issues

This brief summarises the most urgent economic issues which the Government will need to tackle in the next few months. They are:-

(a) The Budget. The last week of May and the first week of June are not available because of the Bank Holiday and the recess for the European elections. Present Treasury thinking is that the best date is 12th June. A Budget before the European elections would be too soon for the new Chancellor to prepare and for colleagues to take any related decisions. But to leave matters much after 12th June would leave too little time for the passage of the Finance Bill. I am giving you a separate brief on the broad issues which will arise on the Budget.

12th June ✓
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(b) The CAP Price-Fixing. Negotiations will reopen in May. The outcome is important, among many other reasons because it affects the net payments we will make to the Community Budget over the next 12 months.

(c) The Public Expenditure Review. Decisions on the current year will presumably be taken in the Budget context. You have more time in which to re-examine the inherited expenditure plans for later years. The annual PESC review of expenditure from 1980-81 onwards has already begun at official level. But this is a policy-neutral exercise, confined to three questions: what can be afforded within the already published totals: what adjustments are inevitable for demographic reasons; and what options are available for increases or reductions. You will clearly want to set new guidelines for this operation, and I know that Treasury officials will have draft proposals ready for the Chancellor to put to Cabinet very quickly.

SECRET

If the spending agencies are to adjust their policies in good time for 1980-81, you will need final Cabinet decisions in the autumn - and perhaps before then. The PESC exercise is carried out in 'constant price' terms and there will be a separate and difficult job of setting cash limits for 1980-81. This will be particularly important in the local authority field - see below.

- (d) Rate Support Grant. The annual fixing of Rate Support Grant for local authorities takes place in the autumn. The grant (over £9 billion in 1978-79 always has to be based on assumptions about local authority pay and has important implications for both central and local authority expenditure. Because you will be relying on cash limits as an important element in controlling public sector pay, you may want to give an earlier indication than usual this year of the sort of pay increases to be ^{assumed} ~~announced~~. This points to a decision on the level of RSG for 1980-81 before the summer recess.
- (e) Pay. The "current pay round" ends on 31st July. The original White Paper governing the round ("Winning the Battle against Inflation - Cmnd 7293) is presumably no longer operative but 31st July nevertheless represents a watershed. A number of key problems will arise before that date. In particular:-
- (i) you will want to consider how the Manifesto idea of "more open and informed discussion of the Government's economic objectives" is to be pursued. The previous Government had made a start on similar lines through bilateral talks with the TUC and CBI but had not got very far when the Election intervened.
- || If any new exercise is to have an influence on pay bargaining after 1st August a very early start will be necessary;
- (ii) your Manifesto had a clear line on pay bargaining in the public corporations but still leaves detailed application to be worked out, e.g. some public corporations, such as British Gas, are highly profitable and can "afford" substantial pay increases and

SECRET

others, e.g. British Rail, are permanent public pensioners and cannot, in a strict sense, "afford" to pay wages at all. Moreover pay settlements in some nationalised industries inevitably read across to others, e.g. for manual workers in the gas, electricity and water industries where there are close historical links stemming from their common 'municipal' past. Luckily most of the public corporations' pay bargaining this year has been completed. (The main outstanding case is the Post Office where the offer made has just been rejected by a ballot of the employees.) The reflection of these issues in the Government's financial arrangements with the nationalised industries will require quick examination if a coherent and disciplined framework is to be embodied in the Government's public expenditure plans;

- (iii) Similarly your own approach to pay bargaining in the public services will have to be worked out in detail before cash limits for next year are set.

A fuller brief on public sector pay and cash limits is being submitted separately.

- (f) Immediate public service pay issues. You will be faced almost immediately with the need for decisions on five public sector pay issues: the pay of MPs and Ministers (on which the Boyle Report should be available very shortly); the pay of doctors and dentists (where the Report of their Review Body is to hand); the pay of other "top salary groups" (covering e.g. judges, nationalised industry chairmen, generals and senior Civil Servants) where the TSRB Report is just available; teachers, where negotiations were postponed because of the intervention of the Election (and where the Government has a direct interest through RSG); and the broad mass of local authority white-collar employees whose settlement date is 1st July.

SECRET

- (g) Energy. I have sent you a separate brief covering the energy sector where a number of difficult issues are outstanding. Among the most urgent of these are:-
- (i) Measures to cut oil consumption next winter in order to meet our IEA and EEC obligations. Decisions are needed before the summer recess.
 - (ii) Linked with this is the question of coal. The NCB is heading for a major loss this year and carries a fringe of heavy loss-making pits in politically sensitive areas like Wales and Scotland. Early decisions on these could help reduce losses - next year if not this. You will also need to consider how far you are prepared to pay for extra British coal next winter to replace oil or whether we should import more coal.
 - (iii) The reorganisation of the nuclear supply industry. By common consent the present system will no longer serve and reorganisation is long overdue. Delay will mean setting back completion of the next batch of stations.
- (h) Industrial Issues. There are a number of difficult industrial issues which are bound to come up in the next few weeks. You may care to note the following check-list of the more sensitive of them:-
- (i) The future of the shipbuilding industry (badly hit by the world shipbuilding slump and very expensive to maintain).
 - (ii) The equally expensive problem of the steel industry.
 - (iii) The almost certain early financial collapse of the Port of London Authority.
 - (iv) Possibly the financial problems of Dunlop.
 - (v) Constraints on industrial development caused by planning procedures (the CPRS are conducting a study) - with Moss Morran as the current leading case.

SECRET

- (vi) Regional development with heavy expenditure, doubts about the cost effectiveness of some of the techniques, but continuing pressure for more money. This links with the future of Government support for industry in general and in particular the operation of the Industry Act 1972.
- (i) The European Council. The next regular meeting of the EEC Heads of State and Government is at Strasbourg on 21st-22nd June. The quality of these meetings and the importance of the decisions to be taken varies. But this will be your first appearance and the proceedings are likely significantly to influence at least the atmosphere, and possibly the direction, of EEC policy over the years ahead. We are now the Community's largest paymaster but its third poorest member. There is a lot to play for in terms of redressing this imbalance. I am sending you a separate brief about European matters.
- (j) The Economic Summit. This is scheduled to take place in Tokyo on 28th-29th June. The attenders will be President Carter, President Giscard, Chancellor Schmidt, the Prime Ministers of Japan Italy and Canada, Mr. Jenkins as President of the EEC and yourself. The Summit will be particularly important this year because the international financial situation is still shaky (and has not been helped by the larger than expected rise in oil prices). The Summit provides a good opportunity to urge our partners to react in a sensible manner.
- (k) UNCTAD V. This triennial meeting starts in Manilla on 7th May and may go on until early June. With the MTNs more or less under control and the framework of the Common Fund already agreed, UNCTAD V could create less of a trauma for North/South relations than did UNCTAD IV in Nairobi in 1976. But representation in the final stages is normally at Ministerial level and there will be a good deal of interest in the attitude of the United Kingdom Administration to North/South issues in general and to aid in particular.

SECRET

CONCLUSION

2. There is a great deal to be done in a short time on these issues (and inevitably others will arise in the normal course of business). The most immediately pressing is the shape of the Budget and associated matters like the money supply target. On these you will no doubt wish to await the Chancellor's specific proposals. But close behind in terms of time, and ahead in terms both of intrinsic importance and inherent difficulty, is the development over the months ahead of a strategy for public expenditure. And such a strategy will take you and your colleagues deep into a complex of related issues such as relations with the nationalised industries, the finance of local government and the difficult realities which lie behind the adoption of cash limits for central Government. One essential concern of the Cabinet Office is of course to ensure that the work which clearly needs to be done, and which Ministers wish to be done, is tackled in an orderly fashion and in good time so that the Ministers have a sound basis for decision-taking. This in turn relates to the structure of Ministerial Committees on which I will let you have recommendations when you have made your main Ministerial appointments.

J.H. 4/5

John Hunt