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Policy Unit

*Original returned
to J. Hoskyns*

PRIME MINISTER

THE PAY ROUND DEBATE AND THE "FEAR OF NORMS"

On Wednesday 23 July, E discussed comparability, cash limits and influencing national pay behaviour for the next pay round.

The attached paper examines some of the issues, and conclusions reached, at that meeting.

I have copied it to members of E and other colleagues present, to Robin Ibbs and also to Sir Robert Armstrong.

JH

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JOHN HOSKYNs

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THE PAY ROUND DEBATE AND THE "FEAR OF NORMS"1. INTRODUCTION

- 1.1 On Wednesday, E discussed the closely interrelated subjects of comparability, cash limits and influencing national pay behaviour for the next pay round.
- 1.2 We are in danger of missing an opportunity to influence expectations. A clear message about the pay outturn we wish to see in the public services could be added to the events or announcements (high unemployment, Clegg) which are or will be focussing attention on the next round.
- 1.3 The discussion at E was confused because we were talking at cross purposes about norms. We ended up rejecting the idea of mentioning any figure, because this was seen as constituting a "norm". There was, in fact, no definition of what a "norm" meant. This confused our thinking on public services pay and the extent to which the Government, as principal paymaster, is trying to influence the prevailing mood, rather than allowing itself to be influenced by whatever mood happens to prevail.
- 1.4 This paper attempts to dispel some of this confusion, and suggests that the Government has much to gain and nothing to lose by stating a figure or a narrow band.

2. WERE WE TALKING ABOUT A NORM OR AN OBJECTIVE?

- 2.1 The word "norm" means different things to different people, depending on their past experience and whether they have really thought about it: whether, at one extreme, they see it as a challenge to the unions or, at the other, simply as a stated objective, a desired outcome.
- 2.2 A norm can either be a command or a call for voluntary restraint. A 9% case-by-case public service norm would mean that this figure must be achieved in every public service negotiation, whether voluntarily or by order. The dangers of such a norm are obvious.

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The Government has everything to lose by "issuing orders" which are not readily obeyed and which in some cases could never be enforced. It has a great deal to lose even by making an appeal which is ignored (hence our repeated advice that anything which sounds like exhortation should be avoided).

- 2.3 An objective is quite different. The MTFS itself embodies certain objectives. We are not ordering people to deliver the MTFS objectives. We cannot guarantee their fulfilment. But we have to commit ourselves unequivocally to going all out for their achievement, because that commitment itself makes the achievement more likely. So it is with the cash limits and pay outturns which flow remorselessly from the commitment to MTFS.
- 2.4 If we don't answer the question, "What would the Government like to see as the pay outturn for the public services?" we are effectively saying that we do not know what the implications of the MTFS are for cash limits and pay; or else that we know, but for some reason will not say.
- 2.5 We have already agreed, internally, our objective for the aggregate outturn. It is 9%. Is that figure roughly right (leaving aside for the moment whether it is attainable)? Does it fit the M_3 targets and the MTFS? The next Section looks briefly at this question.
3. HAVE WE GOT THE IMPORTANT NUMBERS RIGHT?
- 3.1 If this 9% objective is to apply to pay outturn, then it must broadly apply also to cash limits, of which pay is the major component in most cases. It must therefore, by extension, apply to the Government's total expenditure of £98bn (1980/81 cash). If it does not do so, then the public sector is not bearing its share of the monetary deceleration. A 9% increase on £98bn is £8.82bn. But about £34bn of that (most transfer payments plus defence) will be fully-indexed. As we understand it (and we may have got this wrong) the "forward-looking" basis for this indexation is really backward-looking. The past year's RPI increase is applied "forward" to the coming year. If this is correct, and if we assume 15% rather than PESC 80's 17%, this £34bn would be increased by £5.1bn. Thus, only the difference (£8.82bn-£5.10bn), ie £3.72bn, would be available

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for increasing the un-indexed balance of £64bn. That £64bn could therefore only increase by 5.8%. If we regard other parts of public expenditure (eg health and education) as effectively indexed as well, then the increase available to the un-indexed part becomes much smaller.

- 3.2 If our concern about the indexation of large parts of public expenditure is based on a misunderstanding, then no new problem arises, and we can go straight onto Section 4 below. If, however, we are right, then not only are we talking about a public services pay outturn objective of less than 6%, but other more fundamental questions about public expenditure arise. The indexing problem (if it is a problem) stems from an almost unquestioned assumption that the Government is merely another participant in the economic process, and must therefore protect itself against inflation as best it can, just like any private party. This can't be right.
- 3.3 Perhaps we will eventually have to consider turning the whole process upside down: doing all the forecasting in cash terms, based on forecast inflation, as in PESC 80; establishing cash limits, in exactly the same way as the monetary targets in MTFPS; adjusting cash limits downwards only, if inflation turns out to be lower; but not upwards if inflation turns out to be higher.
- 3.4 In our paper on "Public Sector Pay" of 18 July, we said:

"It won't even be possible to say what a realistically achievable result is, until that team has done the sort of thinking suggested in this paper "

If the above analysis is right, the task is more daunting than we had realised. But that is not an argument for not doing some preparatory thinking, on the grounds that "grand strategies never work" etc! If we are about to scale Everest single-handed without oxygen, we might as well know before we start.

4. THE E DISCUSSION WAS ABOUT NORMS NOT OBJECTIVES

- 4.1 The conclusion of E assumed that any number used would be a norm, a "command", amounting to a brittle, all-or-nothing strategy. At its

simplest, our thinking consisted of three propositions:

- "1. We tried a norm last time and it ended in disaster.
2. Anything which involves the Government stating a number is a norm.
3. What is being suggested here involves stating a number. Therefore it's a norm. Therefore it will end in disaster."

There was reference to the miners in 1974. But that was a different situation involving a definite norm, for the whole country, and a near-monopoly nationalised industry, in the immediate aftermath of the first massive OPEC price rise. In the coming round, there would be no norm, no formal national pay policy, nearing the end of its tether; money supply would be decelerating not accelerating; RPI falling not rising; very different trade union attitudes; a greater readiness by employers to ballot (in the public services too, if we try); £12 deeming. But Government would state an objective for aggregate public services pay. Almost everything that matters would be different. We really have to think carefully before concluding that we are comparing like with like.

4.2 It was suggested that it would be easier to mention the figure in a couple of months' time when we have "a better idea of what the pay bargaining climate will be". But are we trying to set that climate or simply respond to it? We suggest that, since the Government is disposing of £98bn in the current year, of which public services pay is £32bn, and another £34bn is indexed, the Government is the climate - or a large part of it.

4.3 There is, of course, a case for preserving flexibility so that the Government does not nail its flag to the mast for a precise figure in a particular negotiation, where even marginal defeat is seen as a blow to the Government's credibility. We must have flexibility in order to move at the margin, both under negotiating pressures and under supply and demand requirements. But we're not, in any case, proposing a deliberate and rigid challenge. We are proposing that we should state an objective, a desired outcome, and then conduct the debate in such a way that trade union threats or promises to exceed that figure, far from becoming evidence of virility and

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leadership, become marks of shame and stupidity, incurring public odium.

- 4.4 It has frequently been said, at E meetings, that we wish to see a "scatter" of outcomes, as greatly preferable to a single figure. Why? In the event, we certainly will get a scatter, because we would be using our flexibility to drive down the weak bargaining units in order to compensate for surrender to the strong ones. But we shouldn't fall into the trap of thinking that such a range of outcomes proves the existence of a market. A real market would certainly produce a range of outcomes; the reverse is not true! In the public services, except at the margin and in particular areas where the employer is free to try to match supply and demand, the scatter of outcomes is evidence not of a market, but of the precise opposite: conflict between more and less powerful labour monopolies.

5. HOW TO USE A STATED OBJECTIVE FOR PUBLIC SERVICES PAY

- 5.1 Even if the objective is "only" 9%, rather than 6% or less, the task is formidable. As we said in our earlier paper:

"We only have to look at Annex A to see what we're up against; the great variety of different bargaining groups, with their negotiations spread right out through the year giving maximum opportunity for each group to search for "upward comparators"; improve its own negotiating technique; make the best use of its disruptive powers."

We still believe that, while efforts at "grand strategy" cannot guarantee success, an unthinking serial approach, taking each case as it comes, without any attempt to think a few moves ahead, is most unlikely to produce an outcome compatible with the MTFS objectives. The fact is that when people do a bit more thinking, they tend to think of things they wouldn't have otherwise have thought of! That's all. We saw this with the decision to reduce MPs' pay to less than 10%. We came very close to missing this opportunity as a result of not thinking our way through to the 9% objective for public services pay early enough to influence our thinking about the TSRB. We then had second thoughts - fast.

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- 5.2 This paper proposes that negotiations should be dealt with, case by case, but with an overtly stated objective for the pay outturn, which the Government cannot enforce, but hopes to see and will try to achieve, so that all parties know the ball park in which the employers will be negotiating, and the economic justification for it.
- 5.3 E's present position is that there should be case-by-case negotiation but with no publicly-stated pay objectives. We regard this as an unsustainable position. First, a number or a narrow range is bound to emerge sooner or later, and is indeed already doing so. Second, if the Government continually refuses to acknowledge such a number, it appears not to know what it's doing, or else to have decided to follow events, rather than lead the way in changing expectations.
- 5.4 If there's going to be a figure, make sure it works for us
- 5.4.1 We should be using the high unemployment figures, and the dissolution of Clegg together with a stated pay objective, to do two things: first, to open up the debate and change attitudes especially among public service workers (whose opinions are never "tracked" by their employers, we would guess); second, to establish clearly that the last pay round is now over. This is important, because with an "endless belt" of 11 months, it is very difficult for the public to realise, for example, that the British Telecommunications 20% increase belongs to the same pay round in which the local authority manuals settled last November for 13%.
- 5.4.2 What the debate can cover. Here are some of the messages which can come over during the debate:
- (1) The less we spend on public service pay, the more we can do for those who need help (1% on pay translated into hospitals, old people's homes, schools, Youth Opportunities Programme). So those who want to force us to pay more want to take away from relief of unemployment and other hardships.
 - (2) Ensure greater awareness of the net cost of striking. Public service employers can prepare the information. The net cost of the steel strike to the individual strikers should be explained. The media could be encouraged to put across the facts.

- (3) Relate the falling RPI to the Government's strategy and the limits of public sector cash. Show people how the whole thing hangs together. They either help to make it work faster, or try to stop it working. Which do they want? Which do their union leaders want? Why?
- (4) Heighten the conflict of interest between public sector and private sector workers. Point to the lower settlements, the mounting bankruptcies and unemployment in the private sector. Open up the moral issue for public sector workers in strong positions. How do they justify their high claims? Where is the money to come from? Which weaker groups will have to pay for it? Is it fair?
- (5) Expose the intellectual and moral bankruptcy of the trade union position. The greater the rumpus, the more damage they tend to do themselves, provided we are prepared to take them apart, honestly and objectively, when they talk nonsense. For example, on television on Tuesday, Len Murray argued that high pay was not the cause of Britain's problems. He then said: "If high pay was the cause of the problem, Germany would be flat on its back by now". He was allowed to practise this deliberate disinformation, despite the responsibility of his position. No-one in Government or the CBI challenged him. No-one asked him whether he really meant that German workers were more productive because they had higher pay, rather than vice versa. This sort of rubbish will continue as long as it is not challenged.
- (6) Answer "what if" questions about inflation and unemployment, for different levels of pay settlement.
- (7) We can deliberately take out insurance against failure to achieve our 9% outturn by frankly admitting that we can't win them all; that there are some groups with enough power, if they are sufficiently unscrupulous, to get a higher settlement paid for by others. This achieves two things: first, it insures against our staking everything on case-by-case success; second, it puts increasing moral responsibility on powerful groups and, by close association, on the unions

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in monopoly nationalised industries whose pay settlements we are not trying to curb directly, but which can have serious knock-on effects in both the public services and the private sector. But this moral pressure can only work if the Government shows that it does care about the human aspects of unemployment.

6. MISCELLANEOUS POINTS

6.1 Public service expectations

6.1.1 In our next opinion research, we will be checking to see what public service workers are expecting in the next pay round. At an anecdotal level, we happen to know that in one particular fire station, the general expectation was that the Government would impose single figures on firemen, as it had done on MPs.

6.2 Greater synchronisation of pay bargaining in the public services

6.2.1 There was some discussion of this at E. The difficulty of preventing leapfrogging, with a year-long public services bargaining process, is increasingly recognised. For example, the following large groups would all be negotiating at the end of the coming pay round, so that their actual awards will run well on into the following round when we would be hoping for settlements to be lower (in other words, there is already an element of "backward-looking" for these groups): Civil Service industrials (July); NHS nurses and midwives (April); local authority non-manuals (July); British Rail (April).

6.2.2 Greater concentration of bargaining, over a shorter period, might also give trade unions less excuse for not doing something more positive with the rest of their year.

6.2.3 In recent opinion research by CRD, the following question was put and answered at our request:

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"It has been suggested that a law should be passed which would make it necessary for pay talks for everyone to start on a fixed date and be finished by a set date, a month later. Do you think this would be a good idea or a bad idea?"

	<u>All</u>	<u>Con</u>	<u>Lab</u>	<u>Lib</u>
	%	%	%	%
A good idea	70	69	72	73
A bad idea	21	23	19	23
Don't know	10	8	9	5

These answers suggest that there is a strong desire, non-party political, for order instead of chaos in pay bargaining. This need for order is the reason why incomes policy is often electorally popular, even if economically disastrous. Synchro-pay happens to be something which is both electorally popular and - subject to any thinking that has been done on the topic - economically sensible.

7. CONCLUSION

Slowly but surely the size of the public services pay problem, and the numbers we should be aiming for, are coming into focus. It would be a pity to stop the thinking process just at the point where the size of the problem is apparent, but the tactics and mechanics for solving it are not.

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