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Prime Minister

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Qa 05026

*copy to Analysts
Mr. Walker*

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To: PRIME MINISTER

From: J R IBBS

Public Sector Pay Policy

I agree with Mr. Ibbs that we must go for what is possible. But we will pay a heavy price - politically and economically - if public sector pay goes up faster than in the private sector in

1. During yesterday's meeting on Public Sector Pay I became concerned lest desirable changes envisaged should go further than actually would be attainable in the negotiating situations likely to exist in the coming pay round. I offer the comment as somebody who has hitherto faced rather similar problems as one of the parties in a negotiation.

the next round (as per 5)

2. I start from the point that the purpose of any proposed changes is to support the main strategy of reducing inflation. I agree that demonstrable progress on reducing inflation depends on pay settlements generally becoming lower and that the public sector must be brought down as strongly as is possible; the private sector cannot be left to achieve the necessary reduction on its own.

Suggests it might be...

3. Obviously if comparability as the basis for a settlement can be replaced by collective bargaining with reasonable confidence that it will result in a lower outcome, then such a change is desirable. (This is particularly so if it also permits greater flexibility to take account of the forces of supply and demand.) Similarly if an unsatisfactory method of assessing comparability can be replaced, in instances where the introduction of negotiation is not feasible, by a more soundly based method, then the change should be made.

4. However, if the reality is that the forces and attitudes that would exist in a collective bargaining situation are likely to lead to a higher settlement, then a comparability system is probably preferable. Again, if revision of a comparability system is unlikely to be successfully negotiated, it may be better to stick for a while with the imperfect arrangement. These considerations appear particularly important during the crucial period when rising inflation has to be reversed and replaced by falling inflation. At this time it is important to win negotiations and to succeed when imposing changes. Failure to do so will extend beyond the immediate issue and damage the whole approach including the concept of cash limits. Once downward momentum has been achieved, greater risks can be taken in negotiations and in attempts to correct comparability arrangements.

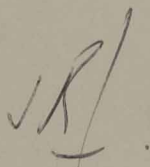
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5. I emphasise that I am not against driving down public sector pay as strongly as great determination can achieve. However, the test in each instance should not just be "is the change in method or the specific reduction in settlement desirable", but also "can it be achieved?". Any trials of strength need to be those which can be won. Provided public sector pay falls, it will not matter unduly if initially the decline is a little less than that in the private sector where the forces that can be imposed by monetary policy are greater.

6. I believe these arguments apply both to the public service sector and to the nationalised industries. I agree that as much pressure as possible must be brought to bear on the latter through cash limits but these cannot have quite the same force as potential bankruptcy has in the private sector.

7. Because I believe that success will depend on what is in the minds of the negotiators; on their attitudes and behaviour; I wholly support the Chancellor's wish to do everything possible to influence these through all the means at the Government's disposal.

8. I am sending a copy of this minute to the Chancellor and to Sir Robert Armstrong.



20 May 1980

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