

Ref: A0212

SECRET

PRIME MINISTER

Proposals for the years after 1980-81  
(C(79) 35)

BACKGROUND

The provisional programme for decisions on public expenditure after 1980-81 is to have a 'Second Reading' debate this week; for the Chancellor and the Chief Secretary to conduct a series of bilaterals over the next few weeks, in parallel with the separate talks the Lord President will be having about Civil Service Manpower; and for the results to be reported back to Cabinet at the first meeting after the Party Conference - 18th October. Almost certainly you will need a second meeting, probably on 25th October, to complete the process. The Chancellor would then bring forward a draft White Paper, including some economic background, in about the second week of November. Publication would follow before Christmas.

18th  
25th

2. This paper is the starting point. It covers only part of the story: there is a separate paper on Nationalised Industries, C(79) 37, and also a paper from the Lord President on Manpower Savings, C(79) 38, for which some credit is taken in this paper. The Chancellor's target nominally remains the one he set before the holidays: to reduce public expenditure, by 1982-83, to the level of 1977-78. In fact the figures in Annex C show him to be aiming a little short of that target - by £380 million in 1982-83 and £660 million in 1983-84 - after taking account of the suggested savings in his present paper, those proposed for the Nationalised Industries and a contribution from staff savings. These shortfalls are not particularly meaningful (they could e.g. be more than wiped out by a reduction in our EEC contribution) but emphasise the need not to accept any significant relaxation from the overall levels of saving proposed.

3. In theory this week's discussion could be short and largely procedural with the main battle reserved until after the bilaterals: and you may well judge it best to try to rail-road the Chancellor's paper through on that basis.

Prime Minister

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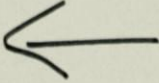
See also Mr Edwards' paper (attached), which asks for special treatment for trades - not very convincingly.

PL  
12/9



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4. Nevertheless I think the Chancellor's paper is vulnerable on two separate scores. Even if, therefore, you are going to give him your full support I think you ought to be warned about them and of the answers you could make to colleagues who are reluctant to agree.



5. The first vulnerable point is that the paper contains no real assessment of the future prospects of the economy. The Chancellor will claim that forecasts based on the present Treasury model are of little relevance because the new economic policy will create a new dynamic which the model, based on past relationships, cannot properly reflect (although I gather a second run was done which postulated quicker and more favourable reaction to the Government's budgetary measures). He may, if pushed, say that, were the medium-term assessment (MTA) to be brought into the reckoning, it would support the need for severe restraint in public expenditure of the kind he has outlined. But his basic approach will be that the reduction in the burden of public expenditure is a pre-condition for success in the new economic policy and that the cuts he is asking for in public expenditure over the next five years are justified in their own right and irrespective of any forecasts. I think this argument is sustainable. What is harder to answer - without reference to an MTA - is how much difference it would make if the cuts were phased differently. If discussion develops on this point you may want to support the Chancellor by reminding colleagues that the last Government's plans repeatedly went awry because they committed expenditure on the basis of forecasts which were invalidated by events, and that the only prudent course is to take a tough line on public expenditure now. The time to think of spending more money will arise when we have earned it. This need not preclude the Cabinet from having a general discussion on economic prospects at some convenient date in the future but it would be a mistake to think that such discussion would be likely to ease the task which Cabinet must now face.



M.P. - Claims -

Programme  
Agri-industry  
Miss  
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- D.E. - don't disagree.  
- Scot.  
- Ed. -  
- DOE -  
- Dep 10/10/84  
- Scottish  
- S. I. ed  
- Ch. P. 10/10/84

78-9, 3-4

214

6. The second vulnerable point relates to priorities. The Chancellor has divided the programmes into three categories: 'priority'; 'difficult to reduce'; and 'bearing the burden of adjustment'. Because so much weight must fall on this last group, some members of the Cabinet may want to reconsider the over-riding priority it has hitherto given to Defence and to Law and Order. They may argue that, while it was right to reverse the relative decline of Defence at the beginning of the Government's life, the continuation of this priority through the life of a Parliament is unnecessary and unfair. Similarly with Law and Order. This argument becomes the stronger when you look at the implications for some of the non-priority programmes (e.g. education and Northern Ireland). The only possible answer to this seems to be that no-one should argue that the Government should abandon its priorities now. Equally, however, no decision now can be binding on discussions in future PESC years when adjustments either way to any programme will be open in the light of developments. But this will only serve to emphasise the tentative nature of the White Paper and to increase the difficulties with e.g. the local authorities.

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Cuts  
Consumption

HANDLING

7. You might invite the Chancellor to introduce his paper, and see whether the Chief Secretary wishes to add anything on the detail.

8. You might then see if you can get quick agreement to the overall objectives. Presumably colleagues will confirm that they still want to get expenditure down to 1977-78 levels, especially given the Chancellor's judgment that his proposals are the minimum compatible with the objectives of bringing down inflation and reducing the tax burden. But it would be as well to be sure. Thereafter your aim in the discussions might be to end up with a clear instruction to the Chancellor and to the Chief Secretary to get as much as they possibly can towards the target in bilateral discussions so as to minimise the area of uncertainty to be resolved at Cabinet in October.

Stabilise  
Cuts in  
unproductive  
programmes  
in priority  
for  
In view of  
of cuts in  
social services.



SECRET

9. You will then want to run briefly through the individual programmes described in paragraphs 17-31 in order to see how far you can go in chalking up the agreement of the Ministers concerned to the particular proposals made by the Chancellor. You will want to avoid detailed discussion on any individual programme. This will be for the bilaterals. But to the extent that individual Ministers accept the Chancellor's arithmetic as it concerns them the easier will the bilateral process be.

10. You may then want to look briefly at the Contingency Reserve (paragraph 32) in order to get collective agreement on this.

11. As to Civil Service manpower, you will simply need to note that the Chancellor is looking for further financial savings from staff cuts beyond those outlined in his paper. The extent of these savings can however only be assessed when the parallel staff cuts exercise has been completed - a process which will begin under the next item of the agenda.

12. Additionally some Ministers may raise questions about the provision for debt interest, not covered in this paper. Borrowing at present interest rates imposes a heavy future charge, and although this is only a transfer payment not a call on resources, it reduces taxable capacity. Cabinet can do little in the short term to adjust this figure. It may be enough to note that the burden of debt interest is geared to the success of the Government's policies. If these succeed and interest rates fall the Chancellor's (and the Cabinet's) problems will be reduced.

13. Finally, paragraphs 34-36 raise the question of the approach to be made to the Local Authority Associations about the proposals affecting them. Are the Chancellor's proposals acceptable to the other Ministers involved - DOE, Scotland, Wales and Education?

CONCLUSIONS

14. Three conclusions are needed:-

- (i) A broad re-affirmation of the target of reducing public expenditure to about the level of 1977-78 by the end of the quinquennium.

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- (ii) An invitation to the Chief Secretary to discuss with all the main spending Ministers concerned the proposals in the Chancellor's paper (subject to any guidance given by Cabinet on individual points) and to report back on 18th October.
- (iii) Acceptance of the Chancellor's proposals for handling discussions with the Local Authorities about the programmes which affect them.

*John*  
...  
(John Hunt)

11th September 1979