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CABINET

MINISTERIAL COMMITTEE ON ECONOMIC STRATEGY

HANDLING PUBLIC SECTOR PAY IN THE CONTEXT OF CASH LIMITS

Note by the Chancellor of the Exchequer

It is vital that we get levels of pay settlements down during the coming year. It will be appallingly difficult, and the climate will not be helpful. I have no doubt that a sustained policy of fiscal and monetary restraint will achieve a reduction in the rate of inflation, but it will take time and will be painful. Market pressures against inflationary wage and price increases will build up gradually, but immediate reactions to threats of unemployment and loss of profitability may be perverse. Expectations will also be helpfully changed in time, but the present mood of unions and many managements shows how far there is still to go.

2. The Government cannot just meet these difficulties ad hoc as they arise. We must press ahead with our publicity campaigns, and get our message home to employees, unions and managements in the public sector, as well as the private sector. But our main and most immediate contribution will be a rigorous and sustained and publicly understood toughness on the part of public service employers in all pay bargaining. Our record is not good, and there has of course been much confusion in operating the arrangements, commitments and half-commitments we inherited. But

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new bargaining now is going to set patterns for the coming year and for our financial control in the first year for which our Administration will bear full responsibility. We badly need to set a pattern of tough bargaining, and make sure that it is known and understood.

3. Cash limits should help in demonstrating our firmness in pay matters, as in control of public spending generally. But in neither case will they help much unless we hold firmly to them in practice and it becomes generally expected that we will do so. We shall never induce a mood of realism among public sector trade unions unless and until they are brought to accept that their pressures can and will be resisted, or that their members will have to face harsh consequences when/where they are unreasonable.

4. Since this is the beginning of our period of Government and of pay and spending control free of any pay policy, the political, financial and administrative costs of failing to maintain the cash limits we shall ourselves be setting for this year and 1980-81 would be enormous in themselves.

5. The approach I have recommended to the fixing of cash limits for next year, following our general discussion in July, reflects the bolder and more disciplined option which we have collectively preferred, but tries to make as much room as possible for the maximum realism through delaying the point of final decisions. This delay should lead to more realistic limits which it is both more practicable and even more important for us to hold firmly. The approach also demands a firm and consistent line in any bargaining or preliminary discussions before the limits are set.

6. I therefore suggest that:

(a) From the outset we must take every opportunity of ramming home our intentions clearly and forcefully; to those on both sides of the negotiating tables, and to the public at large. But it will be at least equally

important that we are seen to act in accordance with those intentions, particularly and promptly if in the early stages any potential difficulties arise.

(b) We must impose a consciousness of financial constraints on bargaining at all levels. Most of us have blocks of staff and particular pay settlements wholly or mainly within our departmental responsibilities. I hope that we will all individually make a point of identifying the officials and managers most directly concerned at different levels and ensuring that they recognise fully the constraints under which they must operate. Where financial and staff responsibilities are divided, everything possible should be done to bring them into closer contact.

(c) We have already asked officials to examine possibilities for ensuring that those who are responsible for negotiating pay settlements are also made responsible for ensuring adherence to cash limits, and that to the maximum extent possible, this combined responsibility is decentralised so that it is exercised at the operational level. At all levels, from individual Ministers down, our aim must be that costs of any settlement which exceeds what the cash limits will cover are offset by the responsible departments and managements.

(d) We have to recognise the dangers of unions playing off individual departments, managements and industries against each other. It would probably make sense, therefore, to encourage/require all public sector employers to notify us in good time of the developing pay situation in their field and of the pay offers they are likely to make. These offers could be reported centrally to the Treasury, the Department of Employment and the Civil Service Department, who would jointly ensure that any particularly "expensive" or serious threat was rapidly brought to the attention of their Ministers. This could be of particular value during the period before we have finally set the

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cash limits. There is, however, a danger that such a system might develop into an arrangement for authorising settlements which cannot be afforded. Industries and departments would have to remain responsible for financing themselves, within the relevant cash limits, any offers they propose to make. Even so, it is probably right to proceed with arrangements of this kind.

7. I invite my colleagues to endorse the foregoing suggestions and take appropriate action to follow them up.

H.M. Treasury
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(G.H.)

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