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PRIME MINISTER

Nationalised Industries' Cash Limits and Performance Targets
for 1980-81
(E(79) 35)

BACKGROUND

This paper runs parallel to the one on Cash Limits for Central and Local Government (E(79) 34) which is also on the Agenda. But the nationalised industries are in a different situation, operating in a commercial environment, and with a financing requirement which is the product of a good many factors: Revenue; Expenditure; Investment; etc. Cash Limits are thus a much less precise instrument, and more difficult to bring to bear in pay negotiations. Conversely, managements have a lot more flexibility in adjusting the other components to accommodate pay increases. The Committee considered all these points in July, when it agreed (E(79) 4th Meeting) to extend the 'Option A' approach to the nationalised industries, by setting cash limits which would impose some discipline on pay negotiations. This approach is entirely consistent with the Government's other plans for future relations with the industry, which are being considered separately by Sir Keith Joseph's Group.

2. Like the other paper (E(79) 34) before this meeting, the present paper seeks decisions on method, and proposals for precise cash limits will come up for approval later in the autumn.

HANDLING

3. Two groups of Ministers are involved. You might start by asking the main protagonists - the Chancellor, the Secretary of State for Employment and the Secretary of State for Industry - to speak generally. You could then call on the Ministers concerned with individual industries (for the most part, represented by substitutes on this occasion). Those involved are: Mr. Moore (representing the Secretary of State for Energy); Mrs. Oppenheim (representing the Secretary of State for Trade); ~~Mr. Kenneth Clarke~~ (representing the Minister of Transport) and, on a small scale, the Secretaries of State for Scotland and for the Environment. [The Secretary of State for Defence, if he stays for this item, may wish to raise a point about the Royal Ordnance Factories - see below.]

CONFIDENTIAL

4. The following main points seem likely to arise:-

- (a) The 'Option A' Approach. Ministers were broadly satisfied last time that this should be extended to the nationalised industries. Nothing in this paper throws any serious doubt on the earlier decision. Consultation at official level does not suggest any major disagreement.
- (b) Setting the Limits. The Treasury propose starting with a 'rule of thumb' that the increase in pay should be somewhat less than the expected increase in the RPI. This would then be worked out case by case for the individual industries. The paper discards the alternative approach of deriving pay increases from the target increases in money supply. (I'm sure this is right: but it is odd to find the point arising almost casually in a paper about nationalised industries, and not in the main paper on cash limits.) Broadly speaking, the rule of thumb would put a lot of pressure on coal and rail, and probably on Posts; but would cause little problem for gas, electricity, airways, or telecoms, where substantial productivity gains can be foreseen and where, apart from airways, a good deal of price flexibility is available. In the case of steel, all this is swamped by the very much larger economies being sought in the run-down. You might guide the Committee broadly to approve this 'rule of thumb' approach, subject to seeing how it looks in its application to individual industries.
- (c) Particular Cases. You will want to discourage detailed discussion: these issues will arise later. But there are some particular points which may come up. On coal, it will be very important to make sure that Mr. Howell (when he gets back from Brussels) circulates his paper on Coal for the E meeting on 27th September. This paper will touch on the initial response to the NUM pay claim. This reply may well have to be made before cash limits can be set for the NCB. But the tactics are, I understand, to defer any positive response until much later in the year, despite the NUM claim for restoration of the 1st November settlement date. Mr. Howell must carry his

CONFIDENTIAL

colleagues with him on this key negotiation. Mr. Howell (and in his absence Mr. Moore) should also consider how the rules should apply to the Atomic Energy Authority: is it to be treated as a nationalised industry, or does it fall under the Central Government procedure already discussed under Item 1? (The latter seems appropriate.) Finally, the Secretary of State for Defence may suggest that the Royal Ordnance Factories should be treated by an analogy with the nationalised industries. The analogy is not exact. In any case, the Cabinet has already commissioned work on decentralisation of Civil Service pay negotiations, which is especially relevant to MOD's problems. You will not want to anticipate the results of that review.

- (d) Procedure. There should be no difficulty in agreeing that the Chancellor should come forward at the end of October with specific figures, following discussions among officials and with the industries. (In practice, the Agenda is likely to be very crowded at the end of October, and the decisions could slip into early November; but you might say that it is important to have proposals ready before the end of October.)
- (e) Information Flows. The Chancellor makes specific proposals for keeping in touch with pay negotiations and monitoring cash flow in the nationalised industries. Here he is in dispute with the Secretary of State for Industry (the exchange of letters is annexed to the paper). Underlying this disagreement of principle is a particular case. It concerns the UPW settlement, where apparently the Post Office agreed to re-open the postal workers' pay settlement, without telling the Department; breached the cash limit in consequence; and left it too late to take account of this in the recent round of postal charges increases. The Secretary of State for Industry is about to write to you and other Ministers, suggesting corrective actions. You may not want to get drawn into a discussion of the particular case; but it underlines the need for fairly close contact with the industries, despite some Ministers' wish to disengage completely from pay

CONFIDENTIAL

negotiations and rely wholly on cash limits. It is no use relying on cash limits if the industries choose to disregard them.

- (f) Presentation. You might ask the Chancellor to consider, before the next meeting, just how these cash limits would be presented. Would the Government explain the rationale of the 'rule of thumb'? or would it say that it could only afford so much (£X million) for nationalised industry finance, and that the industries must find the rest themselves? Or would it say that it had set a cash limit appropriate to the circumstances of each individual industry, and try to avoid a detailed discussion? The public stance is important, as the Chancellor himself recognises in his 'general' paper (C.6(d) of E(79) 39).

CONCLUSIONS

5. I think the conclusions could follow those set out in the Chancellor's covering note (paragraph 10 of E(79) 35);

- (i) To agree, for the purpose of discussions with the industries, the 'rule of thumb' and 'broad approach' set out in the paper.
- (ii) To agree that discussions should now begin with the industries on the make-up of the 1980-81 cash limits on the lines set out in the paper.
- (iii) To invite the Chancellor to bring forward proposals for cash limits at the end of October; and that these proposals should extend to presentation as well as substance.
- (iv) To agree that the nationalised industry chairmen should inform Ministers of their intentions before beginning pay negotiations; that arrangements for monitoring cash flows should be strengthened as necessary to make cash limits stick; and to ask the Chancellor to arrange for this in consultation with other Ministers concerned.

J.H.

(John Hunt)

19th September 1979