

FROM: THE RT.HON. SIR KEITH JOSEPH, Bt, MP



KJ/SMC

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22nd August 1977

I have read, with admiration, the draft economic paper.

There are only 4 pages - 12-15 - with parts of which I have strong disagreement.

I attach a suggested insert in pages 12-15 in substitution for some of your existing drafting.

I am not sure that there are enough references to Europe.

For the rest, I have a number of drafting points, which I have set out on a separate sheet.

I am sending copies of this to Margaret Thatcher, Geoffrey Howe, Jim Prior and Chris Patten.

C.c. Rt.Hon. Mrs. Margaret Thatcher, MP ✓  
Rt.Hon. Sir Geoffrey Howe, QC, MP  
Rt. Hon. James Prior, MP  
Chris Patten - CRD.

Re-entry to free collective bargaining from a period of controls is bound to be unpleasant. The distortions caused by the policy have to be unwound and, people want them unwound at once.

But this time there are two entirely new factors. First, it is now common ground that money supply must be kept on a tight rein. Monetary contraction, that is keeping the rate of increase in the money supply lower than the current rate of inflation - does not stop a temporary surge but it does prevent a continuing rise in inflation. If the monetary contraction is steadily and gradually maintained until the rate of growth in the money stock equals the rate of growth in the supply of goods and services, then inflation will gradually be abated. That is one important, indispensable new factor. It is not a panacea. It is difficult to apply - especially when we swing, because of oil, from balance of payments surplus to a balance of payments deficit.

Secondly, there is the new factor of cash limits in the public sector. It is true that the capacity of trading services - such as the nationalised and subsidised industries - and of other parts of the public sector to raid other sources - profit,

investment funds, the consumer through higher prices - to support the wages bill has not yet been tested.

But these two factors together give hope that, properly and continuously explained, as the government has not yet done, they can change the outcome of re-entry.

Of course, with freedom to bargain there will, and should be, a wide range of different increases for different groups. Employers, public and private, are in an infinite variety of different market positions. Some face strong demand at home and abroad: some face weak demand: some need more of one sort of labour: some need less: some have adequate profits in real terms for survival and even for necessary expansion and investment: some have not.

The same diversity applies to managers and workers. Some are in short supply: some are not. Some can increase productivity more or less sharply, so as to absorb part or all of increased pay: some can or will not. Some have strong bargaining positions: some do not.

All these factors in combination - money supply, cash limits, profits, productivity, pay

claims, the market - mean that there is a link between unit labour costs, prices and jobs. It is <sup>the</sup> reality of this link which needs to become widely understood and accepted.

The reality is certainly now understood and accepted by government ministers though we blame them for only spasmodically and in part spelling it out.

It is crucial that the reality should not be obscured by the government stepping in between an excessive wage claim and the consequence in loss of jobs, either by relaxing its money supply targets or by increasing cash limits or subsidies, or by shifting investment funds to earnings or by rescuing private sector companies crippled by excessive unit labour costs.

*No*

We recognise as the Government does - that there will be widely differing pay increases. Suitable pay increases, for instance, for the Police - where an expansion in our view is necessary - and for some other groups, will have to be offset by not only lower increases for most other people, but much lower increases for those groups where there is no shortage or where profits or cash limits are a particular constraint.

It will be said that since all have suffered from prices, therefore all should be protected from them. It is precisely that philosophy, at a time when our national income has fallen because of oil prices and has not been restored by growth, that has led to our present troubles.

Moreover, many of the groups which will do less well in the immediate future, have been more than protected over recent years from the effects of inflation. Some groups there are, particularly managers and some professionals and those retired with savings, who have suffered savagely over recent years.

It will also be said that it cannot be right to reward those more who have stronger bargaining power -either because their skills or labour is in short supply, or some other reason. But there are really only two broad choices in settling pay. One is to recognise the realities of supply and demand and to rely upon pay differentials for skills, responsibility, etc. and the other, to refuse to recognise the market and to be forced, as a result, either to accept more and more shortages, inefficiency, strikes, distortions, disruptions or to move towards direction of labour.

COMMENTS

Page 1 - I found a shade optimistic. Inflation and the various manifestations of hostility to enterprise do, together, make things much worse than in 1951 - and there is no turnaround in the terms of trade to be counted upon.

Page 3, 9 lines from the bottom

Before "taxation" insert "personal"

Page 5, lines 3 & 4

perhaps omit parenthesis

Page 6, para 2

Perhaps insert - since we want to avoid upsetting the big organisations unnecessarily - "we have learnt the lessons that however indispensable the large units are ..... lean the other way ....."

Page 7, line 5

After "spending" I suggest inserting "as a proportion of national income", and omitting "prices".

Page 7, VII

Omit "fully and fairly" and insert after "reflect", "demand and supply"

Page 7, IX

Instead of "industrial" insert "economic"

Page 8

Omit first two indented lines and substitute "to continue

Page 8, continued

the gradual contraction in the role of money supply in line with firm monetary targets".

Page 10, para. 3, first three lines

Could we not stress the indiscriminate nature of government housing spending and the need to taper down industrial subsidies?

Page 11, bottom 5 lines

I am not sure what the reference to social services means here.

Page 16, line 5

Insert "productivity".

Page 17, para. 3

Could we insert some reference to "no rescue" - or only in the very, very rarest circumstances.

Page 25, line 8

After "national", insert "average"

Page 26, top para.

Why not add that even India, under Mrs. Gandhi, reduced top tax rates.

Page 36, I wonder whether it might be helpful

to move para. 2 of page 39, slightly expanded, to an

Page 36 cont.

earlier position in chapter 4? The expansion I suggest is "In a world in which new business communities in developing countries, as well as established business communities in developed countries, are increasingly competing with us in every market at home and overseas, we can only flourish if we create conditions which encourage rising productivity, substantial added value and innovation - whether in high or low technology."

Page 36, 6 lines from the bottom

omit "unprofitable industries" and substitute "lack of profit, low productivity".

Page 36, bottom

I suggest to jump straight from the broad arguments and the rest of page 36 to "youth on the dole" is too sharp. Unemployment, as a whole, should, perhaps, come before youth unemployment.

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Page 37

In "the real problem" there is no reference to labour restrictive/practices and overmanning, all under the sanction of the strike threat, which makes us uncompetitive.

Page 37, bottom para, line 1

Omit "industrial" and substitute "business"

Page 37, same line

Instead of "investment" insert, "start, expand, invest".

Page 37, line 3 of same para.

Omit "on the investment" and substitute "on what are generally the savings of other people, often pension funds."

Page 39, para 3, line 1.

Omit "in the world" and substitute "by the British people".

Page 39, bottom para., line 4

Instead of "social policy" insert "the anti-industrial policy seeking to do a social and not an industrial task by methods which, in fact, will weaken our economy and lose more jobs not less.

Page 39, line 5

Omit "cope with this difficulty" and substitute, "facilitate the solutions of these".

Page 41, end of para 1

Insert "moreover it is absurd to spend vast sums of taxpayers' money nominally to encourage jobs on capital-intensive projects, producing very few

Page 41, cont.

jobs indeed on a permanent basis".

Page 41, para. 4, line 1

Omit "we propose" and insert, "in the light of these comments, we propose to remove some of the anomalies. We shall raise ....."

Page 42, line 5

Omit "industrial" and insert "economic".

Page 42, para. 3

Omit first two lines and substitute "these schemes take money from the more efficient to give to the less efficient".

Page 43, para 2, line 2

Omit "be desirable" and substitute "justify money from the taxpayers."

Page 43

I suggest moving para. 5 to follow para 3 instead of para. 4.

Page 46, 3 lines from bottom

Insert "planning"

Page 48, para 1, last line

Insert after "would", "in general".