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FINANCIAL SECRETARY

cc Chancellor of Exchequer  
Chief Secretary  
Minister of State (C)  
Minister of State (L)  
Sir Douglas Wass  
Sir Anthony Rawlinson  
Sir Lawrence Airey  
Sir Fred Atkinson  
Mr Anson  
Mr F Jones  
Miss Brown  
Mr F E R Butler  
Mr Cassell  
Mr Dixon  
Miss Forsyth  
Mr Hansford  
Mrs Hedley-Miller  
Mr Kemp  
Mr Kitcatt  
Mr Lavelle  
Mr Monck  
Mr Unwin  
Mr Widdup  
Miss Peirson  
Mr Burr  
GECS  
Mr Ridley  
Mr Cardona

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PUBLIC EXPENDITURE - LATER YEARS

It may be helpful to offer some quick comments on your minute of yesterday to the Chief Secretary.

2. It was as you say made clear from the outset that any failure to achieve the original Treasury objective in C(79)11 (a phased return to the 1977-78 level of spending by 1982-83) would increase the risk that tax increases would be needed in the next two Budgets. The Chief Economic Adviser's minute covering the Medium-Term Assessment in June concluded that:

"It seems likely that the levels of public expenditure implied in C(79)11 would leave no room for tax cuts in the 1980 and 1981 Budgets. Indeed, even on what must be regarded as extremely favourable assumptions about sales of assets and savings in social security the implication is that taxes may have to rise in these years if the objective of bringing down the PSBR and money supply is to be met."

The first sentence of this was repeated in the Chancellor's July paper to Cabinet on the consequences of failing to achieve the full cuts (C(79)30).

3. It was also made clear that the prospects of securing all these cuts in full were not good, in the view of Treasury officials. You will recall that Mr Butler's minute of 2 August which submitted the proposals for the later years said:

"Cabinet are very unlikely to accept the reductions in full. They are put forward as realistic, but there is always some bargaining, and, where considered necessary, the figures allow for that. To the extent that the Cabinet are unwilling to adopt reductions on these lines, the outcome will fall short of the objective of getting the plans back to the 1977-78 level over the lifetime of the Parliament."

Sir Anthony Rawlinson's minute of 8 August to the Chancellor dealt explicitly with the dilemma we faced. I think that you might like to be reminded of his minute in full, and I attach a copy.

4. We do not recall any suggestion by officials that "the bilateral outcomes were wholly satisfactory" (the Treasury is seldom, if ever, wholly satisfied!). On the contrary: in the preparation and submission of the Chief Secretary's paper for Cabinet on 18 October, reporting the results so far of the bilaterals, we repeated the warning that the expenditure levels resulting were, at best, unlikely to allow any scope for further reduction in the total burden of taxation, and that there was a significant risk, particularly in the early years, that tax rates might need to be raised to contain the PSBR and interest rates. The handling of the bilaterals was discussed among Ministers in September, and in response to the Prime Minister's suggestion that there should have been "an element of bargaining" in the Treasury's approach, Sir Anthony Rawlinson's minute of 2 October explained how the target figures had been reached, by including all the cuts which looked as if they had some chance of proving politically and practically feasible. That minute concluded:

"The perennial trouble is that spending Ministers are almost always reluctant to accept cuts, or forego increases, in their own programmes even though they may endorse an overall expenditure objective."

5. It follows that we are not planning immediately "to undergo the joy of a second cuts exercise". Sir Douglas Wass' minute of 6 October spells out the prospects. On the public expenditure side we are bound to emphasise the difficulty, which must be very clear to Treasury Ministers, of re-opening decisions just taken

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on programme totals whether for 1980-81 (now published) or for later years. We respectfully agree with your conclusion that it will be right to concentrate immediately on not yielding further ground, even though we believe that it will in practice be impossible to avoid conceding some further ground on the extent to which Civil Service staff savings are additional to the cuts already agreed, and on agriculture.

AMB

A M BAILEY

8 November 1979