

Ref. A03993

PRIME MINISTER

The Price Factor in Cash Limits

The Ministerial Committee on Economic Strategy (E) agreed this morning that the pay factor in cash limits for the NHS and the civil service should be 7 per cent, and invited the Chancellor of the Exchequer to reconsider the prices factor in cash limits, and to come back to Cabinet tomorrow if he wished to propose a reduction in the 11 per cent already agreed for the prices factor.

2. I understand that the Chancellor will speak on broadly the following lines. Since the 11 per cent price factor was agreed in November inflation prospects have improved, and 11 per cent would now represent some relaxation of pressure and increased head room. If 6 per cent had been accepted for the pay factor he would not re-open the question, recognising that the room for manoeuvre was helpful. The 7 per cent pay factor will however cost an additional £120 million for the NHS and civil service combined. Reducing the prices factor by 1 per cent would offset that increase by about £100 million.

3. The price factor in the Defence estimates would also be put at 10 per cent. Cabinet have, however, agreed (as the price for securing the Defence cuts) that both the pay and the prices factors for Defence are open to revision. The Chancellor is not going back on that undertaking.

4. He will also agree to consider any exceptions which colleagues might propose on the ground that public faith is already pledged to outsiders. One likely example is the Arts Budget.

5. There will be no changes for the local authorities or the universities where the factors of 6 and 11 per cent have already been announced.

6. Other Ministers are likely to argue that the prices factor should be left at 11 per cent for all cash limits, on the ground that the revised forecasts for inflation do not suggest a figure significantly lower than that, and that departments will in any case still need head room in which to accommodate the difference between a 7 per cent pay factor and pay settlements inevitably not lower than $7\frac{1}{2}$ per cent.



SECRET

7. The Chancellor is also likely to reopen the question, discussed at E this morning, when the 7 per cent pay factor should be publicly announced. The Treasury's difficulty is that it has to be incorporated in well over 100 separate votes. This means that civil servants in all Departments will be seeing the figure and so it is bound to leak. The choice, as seen by the Treasury, is between announcing it or seeking some excuse (which they would not want to do) for deferring publication of the Estimates beyond Budget day. An early announcement would be undoubtedly welcome to the Secretary of State for Social Services, who wants to get on with his negotiations, but would mean making a statement in advance of the civil service conferences on 28th and 29th January and of the decision on the local authority manuals on 27th January.

HANDLING

8. After the Chancellor of the Exchequer has put his proposition on the prices factor, most of the main spending Ministers will want to comment.

9. If he also raises the question of the timing of the announcement of the 7 per cent pay factor you will wish to hear the views in particular of the Lord President, and of the Secretaries of State for the Environment, for Social Services and for Education and Science.

CONCLUSIONS

10. In the light of the discussion you will wish to record conclusions:-

- (i) on whether the price factors in those cash limits yet to be finalised should be 10 rather than 11 per cent;
- (ii) inviting Ministers to raise with the Chancellor any exceptions which might be made on the grounds that public faith is already pledged;
- (iii) on whether it is necessary to advance the announcement of the 7 per cent pay factor in view of the probability of leaks during the preparation of the estimates.

Robert Armstrong

(Approved by Sir R Armstrong
and signed on his behalf)

14th January 1981