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 Mr. [unclear]  
 Mr. [unclear]* A

Treasury Chambers, Parliament Street, SW1P 3AG  
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PRIME MINISTER

NATIONALISED INDUSTRY FINANCING

As you know, we discussed the problem of nationalised industry financing shortly before Christmas and you asked for an early report from the Treasury on ways in which these industries could become less dependent on the Government for their borrowing. A paper is attached.

2. I think it is important to see this question in a wide context. As we are only too well aware, the nationalised industries present us with a whole complex of problems - the need for greater efficiency in cost control and better services; the need for increased competition, whether through privatisation or through diluting or ending existing monopolies; the pressure for more investment in expanding areas such as telecommunications; and, last but not least, the problem that nationalised industry financing poses for the PSBR. These problems clearly overlap to some degree; they all have financial consequences; and actions taken in one area will have implications in another. But I think that discussion and analysis need to distinguish between them.

3. I think it important as well to remember that as long as nationalised industries remain wholly owned and controlled by the Government, they cannot be subject to the disciplines of the financial markets in the same way as private sector enterprises. Nor could the Government concede them unrestricted borrowing? - the monetary effects could often prove extremely disruptive. Escape from this is in principle only possible by means of privatisation which depends on being able to identify a flow of profits which



can be disposed of in whole or in part to the ownership and control of private investors. If as will often be the case that source of profits is monopolistic, some form of regulation is likely to be needed. For those activities which, for whatever reason, cannot be candidates for privatisation, we must continue to rely on - and strive to make more effective - the present framework of financial targets and performance aims.

4. The attached report focuses, as requested, on questions of finance. I think it demonstrates convincingly that there is no simple answer to be found by just putting the industries "into the market"; and that changes to financing arrangements, unless these are accompanied by other changes of substance, can have only limited effects. Nevertheless, I think that it would be helpful to follow up the questions posed at the end of the paper. In particular, new financing methods such as a possible telecommunications performance bond might embody incentives towards lower operating costs which could contribute towards dealing with some of the other problems.

5. But the most hopeful link of progress may be a new initiative in the general area of privatisation, interpreting this more widely than we have done hitherto. One idea that is touched on in the paper (paragraphs 5-7) is to try to identify areas within the present nationalised industries where it may be possible to involve private risk capital. We need to be inventive. The monolithic character of the state corporations may have to change. Can private enterprise provide some part of the telephone service on the basis of a nationalised main network or run some trains on a nationalised rail network? It is possible that moves like this might both help with the financing and expose the entity to market pressures in a way that would be beneficial. We need to develop these ideas further, not only to cover more industries but to bring about more radical structural changes. We cannot expect the industries to

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help: they are more likely to resist such an approach which will tend to loosen up existing structures. For real progress to be made, the initiative will have to be followed up energetically by the sponsor Departments.

I am sending copies of this minute with the enclosures to Keith Joseph, Robert Armstrong and Robin Ibbs.

*R. Tothier,*

*( Approved by the Chancellor and  
signed in his absence )*

*for, (G.H.)*

16 January 1981

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