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PRIME MINISTER

1981 PUBLIC EXPENDITURE SURVEY

Cabinet is to discuss my paper on this subject tomorrow. I have had contact with a few colleagues about it, and there have been helpful discussions between my officials and Permanent Secretaries and Principal Finance Officers of other departments. My impression is that there will be sympathy for my objective, and indeed for the structure of the proposals, combined with a number of worries and doubts. I thought you might find it helpful to have a note of some of these points, and my reaction to them.

2. It may be suggested that my proposals involve a double squeeze, where expenditure is subject to cash limits. The first part arises from carrying forward any existing squeeze from one year to the next, and the second from the temptation for Cabinet generally to agree in advance on optimistic assumptions about future inflation. My response will be:

- the principle of carrying forward from one year to the next must be the right presumption (I accept - and my proposals allow - that colleagues faced with extreme cost pressures can seek extra cash provision,

/but the onus will



but the onus will be on them to make the case for it);

- I agree tha- there is danger in making unrealistic inflation assumptions. Our assumptions will be for Cabinet as a whole to decide, and my proposals allow scope for reviewing them;
- generally, as my paper makes clear, I recognise that levels of service are politically important, and we cannot push the cash constraint to intolerable levels. But our presumptions should give more weight to what can be afforded, and less to the entitlement to levels of service irrespective of cost;
- it may well be argued that the pressures on spending managers will be such that new techniques will be needed to assist them in meeting cash constraints: greater flexibility in handling Government contracts, pay and conditions of service, handling of shortfall and excess over the end of a financial year. I agree, but we shall have to work these out as we go along.

3. Much worry may turn on the uncertainties of future inflation, and the awkwardness of assumptions which are bound to become public. My comments are:

- I am not at this stage pressing for full cash planning for the later years, beyond the target year (1982-83 in the forthcoming Survey). We can discuss later how far we want to go;
- I do want cash from the outset for the target year, but

/have provided that



have provided that the assumptions we make soon after the Budget can be reviewed, in the light of subsequent events and revised forecasts. Naturally, we shall want to stick to our initial numbers as far as possible. But I fully recognise the need for some flexibility;

- there may be particular worry over pay assumptions. I would like to defer discussion of this until we have numbers in front of us. One possibility is that we may not need to distinguish a separate pay factor in a way which might be publicly embarrassing.

4. I may be pressed to be more open with colleagues in discussing cash revenue prospects, as a natural corollary to discussion of public expenditure in cash terms. I believe this is right. The object is that we should all get a clearer picture of what can be afforded.

5. Finally, I know that some colleagues will be worried about being rushed into a decision of this importance. I have referred already to further discussion after the Budget. I believe it is not unreasonable to ask now for a general decision in principle. We shall have to work out some of the details as we go along, and as I have indicated there will be need of an important discussion after the Budget, when we actually set quantified assumptions as the basis for cash figures for 1982-83. That will be a more appropriate time to go into some of the technical difficulties.

P.S. Jenkins
for (G.H.)

February 1981

(Approved by the Chancellor & signed in his absence).