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SUBJECT.

RECORD OF A MEETING BETWEEN THE PRIME MINISTER AND THE PRESIDENT OF THE CONFEDERATION OF BRITISH INDUSTRY AT 1615 HOURS ON FRIDAY, 13 MARCH 1981 AT 10 DOWNING STREET

Present:

Prime Minister	Sir Raymond Pennock, President of the CBI
Chancellor of the Exchequer	Sir Terence Beckett, Director General of the CBI
Mr. C. Whitmore	
Mr. T. Lankester	

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Sir Raymond Pennock said that he was grateful to the Prime Minister for agreeing to see them at such short notice. Their request for a meeting had arisen out of a meeting they had had with some of their members from the regions the previous day. These members had strongly attacked the Budget, and had requested him and Sir Terence to make plain directly to the Prime Minister the CBI's concern. If the CBI had worries about the Budget, then it was right that the Government should know about them. But this did not mean that the CBI were moving into confrontation with the Government. The CBI were quite simply disappointed that the Budget had given industry much less help than they had hoped. His own reaction to the Budget Speech was fairly typical of CBI members: they felt that the Chancellor's analysis was impeccable, particularly insofar as he had spelled out the growing imbalance between the private corporate sector on the one hand and the personal and public sectors on the other. Starting from this analysis, they had expected some very substantial relief for industry. But in fact, the latter had turned out to be very meagre. The CBI of course welcomed the MLR cut and the announcement of stock relief (though both of these had been more or less anticipated). But these and the other

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minor measures that had been announced did not amount to very much, and as a consequence it seemed unlikely that the imbalance in the economy would be corrected; and industry was likely to be faced with even bigger problems.

Sir Terence Beckett, referring to a note which he handed to the Prime Minister (copy attached), said that the fiscal effect of the Budget was to take money away from industry. The CBI calculated that in 1981/82 industry would be some £550 million directly worse off as a result of the tax measures. This was a very disappointing outcome to all their representations. They were especially disappointed that the Heavy Oil Duty had not been abolished (though they were aware of the complications relating to the Frigg Contract), and that nothing had been done to reduce the National Insurance surcharge. More generally, they felt that a PSBR of £10½ billion in 1981/82 was too restrictive. The Chancellor was estimating the PSBR outturn for 1980/81 at £13½ billion; allowing only for inflation and without any allowance for the effects of the recession going deeper, the corresponding figure for 1981/82 would be £15 billion. Against this background, they felt that a concession on the NIS and Heavy Oil Duty would be justifiable; this would add only an extra £1 billion to the £10½ billion PSBR already forecast, and a PSBR of £11½ billion would - in their view - be consistent with achieving the 6-10 per cent M3 target and a fall in interest rates. Many CBI members had been "hanging on" until the Budget; a number of them would now take the tough decisions that they had postponed in the hope that the Budget would provide some relief. His own view was that the Budget would make the recession worse; it would have been better to have taken some risk on the PSBR than to take the greater risk of a worse recession.

The CBI did not wish to get into a confrontation with the Government. But they had to ask whether there was any possibility of now implementing their earlier recommendations. If not, they would like to press for additional cuts in

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Government current expenditure so as to provide the possibility of a large further cut in MLR.

The Prime Minister said that the CBI's calculation of the direct effects of the Budget on industry was misleading. It did not take into account the extra spending on the nationalised industries which had been announced over the last month or two; it ignored the full effect of the change in stock relief; the figure of £175 million for extra "take" from employers' National Insurance contributions (ENIC) looked rather high; and the calculations failed to take account of the effect of the 2 per cent MLR reduction. As it was, the Chancellor had taken a risk with the 2 per cent cut, and he certainly could not have done it with a PSBR of £11½ billion. The Government had listened carefully to the CBI's representations prior to the Budget, and they had understood that the CBI had given highest priority to a reduction in interest rates. (Sir Raymond Pennock confirmed that this was the case.) The CBI's recommendations on tax would have resulted in a PSBR of about £17 billion, which would have been totally unrealistic. The fact was that mounting public expenditure - the estimated cash figure for 1981/82 was £104 billion - had to be paid for; and that was why taxes had had to be raised.

The Chancellor of the Exchequer said that the CBI's pre-Budget judgement had been that interest rates could be reduced consistently with a PSBR of £12-12½ billion in 1981/82. The decision to go for a PSBR of £10½ billion had been a difficult one, but he and his colleagues had finally decided that anything higher than this would have prejudiced the MLR reduction. Against the background of rising interest rates in other countries, the 2 per cent cut - coming on top of the 3 per cent fall since last summer - should not be under-estimated as a significant measure to help industry.

/ Sir Terence

Sir Terence Beckett said that the tax increases announced, because of their effect on activity, could well lead to a higher PSBR than the Chancellor intended. The CBI were in any case now only looking for a PSBR of £11½ billion, not £17 billion as suggested by the Prime Minister. As regards the calculations, the 2 per cent MLR cut was worth about £500 million, and the £175 million figure for ENIC might be slightly too high; but even taking both of these into account, the Budget would leave industry at best in balance. It was true, as the Prime Minister had said, that the Government had announced extra spending on nationalised industries; but this underlined the fundamental problem that public spending was too high. Even with the additional spending on nationalised industries, the private sector was faced with rapidly rising prices from these industries.

Sir Raymond Pennock asked what had come of the Government's plans to cut back current spending. There was a strong feeling amongst CBI members that, while they were being forced to cut back, the Government was not doing so. He hoped that the Government would find an extra £1 billion in current spending reductions. The Chancellor of the Exchequer explained that he and his colleagues had looked hard for further cuts; but with overspending on certain programmes such as defence as a result of the recession, it had not proved possible to reduce programmes any further.

Sir Raymond also asked why the Government had not dealt with the complication caused by the Frigg Contract earlier so as to make the abolition of the Heavy Oil Duty possible. The Chancellor of the Exchequer explained that the Frigg Contract agreement was in overall terms to the UK's advantage. To make a change with respect to the Heavy Oil Duty would have required renegotiating the whole contract, and this could well have left us worse off. Unfortunately, he had not been able to explain this publicly while discussions were currently going on in the Norwegian Parliament about Statfjord. In response to a further question from Sir Raymond,

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the Chancellor of the Exchequer said that it would not have been possible to have reduced MLR by 2 percentage points and at the same time to have taken two points off the NIS; he had judged that the MLR cut was better for industry than an NIS reduction (only two-thirds of which would have benefited manufacturing industry).

The Prime Minister then asked which type of companies were being hit by the recession. Sir Terence Beckett said that companies of all sizes were affected. Although the Budget had provided some help to small companies, their prosperity was dependent on the success of large companies. Sir Terence reiterated that the Budget was of no net help to industry, and it was not in any way an industrial Budget. The non-nationalised manufacturing sector had suffered greatly over the last 18 months; the Budget had not made their problems any easier.

Sir Terence went on to say that the CBI would like to be able to say to their members that, if the Budget could not now be changed, they would hope for a further MLR cut soon. Without some such indication, many of their members would lose hope altogether. The tightness of the PSBR for 1981/82 suggested that a further MLR cut was what the Government were aiming for; and it would be made all the more possible if there were further cuts in spending.

The Chancellor of the Exchequer said that it would be unwise for the CBI to excite excessive hopes of a further reduction in interest rates. Further reductions in MLR would be by no means easy, and a 5 per cent reduction (which was referred to in the note handed over by Sir Terence) was simply not possible. However, it certainly was the case that the Government were giving top priority, apart from reducing inflation, to getting interest rates down further, and the CBI could certainly tell this to their members.

/ Sir Terence

Sir Terence said that it would help the CBI to hold their members' support for the Government if they could say something on these lines. Although the Government's and the CBI's analysis of the underlying situation seemed to be identical, their view remained that the Budget had been misjudged. He hoped that the Government fully understood their concern; but at least the assurance that the Government wanted to reduce interest rates further was helpful.

The meeting ended at 1740 hours.

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16 March 1981