



*to Mr. Walters  
Mr. Holtzman*

*John Nott, B  
Paper  
Haynes  
mt*

MO 21/8/11

PRIME MINISTER

TACKLING YOUTH UNEMPLOYMENT

I have read with great interest Alan Walters' paper on youth unemployment, circulated by your office on Friday. I am sure it is correct that the institutions of our labour market are not well adapted to adjusting pay rises to what employers can afford to pay young people and that the failure of the real wage to fall is resulting in higher levels of youth unemployment. I believe that more money for the MSC and extending the level of joint subsidised state training for unemployed school leavers is the wrong way of tackling the fundamental problems of the labour market.

① 2. I would support, therefore, more direct and effective measures of reducing unemployment in young persons. The most cost-effective immediate step that I can suggest would be to remove young persons from the scope of the Wages Councils, for an experimental period of, say 3 years. We would thus remove the barrier to employment arising from the obligation to pay minimum wages. There would be no net cost to the Exchequer - even a small reduction, following a cut in the amount of inspection required to enforce minimum wages.

3. The effects would be far reaching. Some 15% of the working population are covered by Wages Councils. I do not have the precise figures for young people but on a pro rata basis some 200,000 youths may currently be affected by Wages Councils' regulations.

② 4. I would also support the idea put forward by Alan Walters for lowering the real price of young labour through changing the National Insurance arrangements. His scheme seems





unnecessarily complex, and it might be simpler to base it on age rather than on income (applying to all youths aged 16, 17 and 18). As with my idea on the Wages Councils, the National Insurance change could apply for an experimental period of 3 years.

- / 5. I attach a letter which I wrote on 11th April 1980 which sets out my thinking more fully.
6. I am copying this minute to the members of E Committee, the Chancellor of the Duchy of Lancaster, the Secretaries of State for Scotland, Wales, Northern Ireland, Social Services, Education and Science, the Chief Whip and to Sir Robert Armstrong.

J.W.

Ministry of Defence

13th July 1981





*From the Secretary of State*

The Rt Hon Sir Keith Joseph Bt MP  
Secretary of State for Industry  
Department of Industry  
Ashdown House  
123 Victoria Street  
London, SW1E 6RB

11 April 1980

*Dear Secretary of State,*

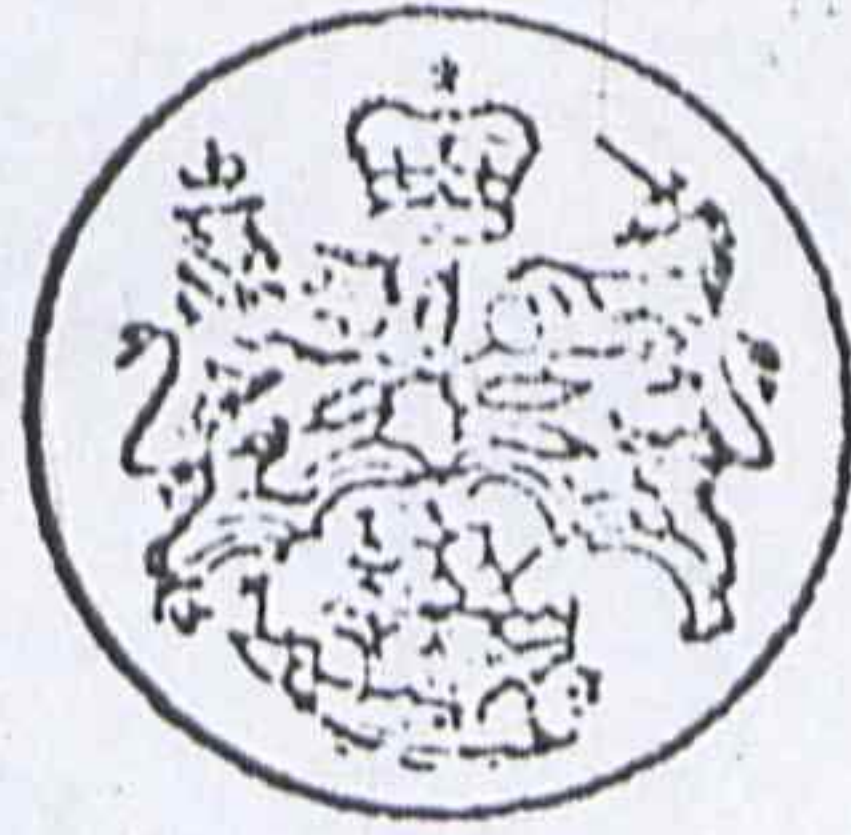
#### WAGES COUNCILS

Jim Prior sent me a copy of his letter on this subject of 26 March to you, and I have seen the report of the review by officials. This issue has far-reaching implications for our economic strategy, and I hope we can discuss Jim's proposals collectively, either in E(EA), if you judged that to be the appropriate forum, or in E if the Prime Minister wished to take it there.

I agree with Jim Prior that we should rule out any form of national minimum wage, and that we have to choose between abolishing the Wages Councils (or at least their statutory powers) and reforming them. In my view the economic arguments are decisively in favour of abolition.

We need to see this question in perspective. We all recognise that the main threat to our economic strategy of squeezing inflation out of the system is that the institutions of our labour market are not well adapted to adjusting pay rises to what employers can afford to pay: and hence that we may see a dangerous rise in unemployment before the strategy succeeds. This means that one of our most urgent tasks is to remove the sources of "stickiness" in the labour market wherever we can, so that pay is more responsive to competitive and monetary developments.





*From the Secretary of State*

Wages Councils, with their statutory power to fix minimum wages for 3 million workers, are only one aspect of this task, but an important one, that does lie in Government control. I do not believe their influence is confined to those workers who are paid the statutory minima. Even though I accept that the Wages Councils follow rather than lead collectively bargained pay settlements, they nevertheless tend to raise the floor on which the structure of differentials is built: and they tend, as the officials' review hints (paragraphs 27-28), to underwrite excessive collectively bargained wage rates in inhibiting competition which might otherwise undermine the market power of trade unions.

We cannot ignore that some of the industries which are prevented by these arrangements from adapting their costs to what their markets will bear are those which are under the greatest competitive pressure even now. For example I receive repeated requests for the introduction of trade protection for the clothing industry, whose employees are covered by the wage determinations of Wage Councils. I cannot grant such requests and have to tell those who make them that it is their own responsibility to keep their costs in line with the prices their customers will pay. But when we ourselves are sponsoring statutory arrangements which inhibit them from doing so, our position is not easy to defend.

It is argued that Wages Councils are there to protect workers who lack access to a competitive market for labour. But this looks like a mere post hoc justification: it can hardly be the explanation for the collection of sectors which Wages Councils now cover (for most of which I am the sponsoring Minister, eg distribution, retailing, hotels and catering and high street services). These are far from the industries in which local monopolies of employment exist, or whose workers lack access to a large and competitive labour market (there is no shortage of shops, or clothing firms). The problem in many of these industries is that the number of jobs is declining:





*From the Secretary of State*

but this is precisely the reason why we must avoid measures which restrict their ability to adjust their costs to what their markets will bear.

Moreover I see that the officials' report finds that Wages Councils are not an effective means of tackling poverty: only a small proportion of the low paid are covered by Wages Councils, and only a small proportion even of these are the main support for poor households, most of the poor belonging to households in which no-one is going out to work. This means we must take even more seriously the danger that statutory wage-fixing reduces the numbers of employment opportunities (especially, as the officials' report says (paragraph 43) for the young and unskilled) and thus tends to exacerbate the problems of unemployment and poverty which we are likely to face in the future.

Clearly we face a dilemma, arising out of the power of the unions to keep real wages and hence unemployment higher than we would wish in unionised industries. This means that in non-unionised industries there is a choice between either letting wages be established at levels that will seem by comparison to be inequitably low, or sponsoring administrative arrangements such as Wages Councils to act as surrogates for trade unions, and thus making ourselves directly responsible for some of the forces keeping unemployment so high.

Whatever the economic arguments, I can see the political difficulty that abolition would entail. It is the statutory powers to set enforceable minima that I think we should be most concerned to abolish, rather than necessarily the Wages Councils themselves, which could have a continuing role as consultative and advisory bodies. But if we conclude that we cannot at this stage remove the statutory powers, then I think we must go for a radical reform of the way they are used, designed to avoid adding to the pressures forcing up unemployment. Option 6 in the officials' report suggests giving Wages Councils an overriding duty to fix wages so as to maximise employment in their





*From the Secretary of State*

industries and hence to take account of market forces rather than to try to work against them. If we are to keep the statutory powers I am sure we need something on these lines.

I am copying this letter to the Prime Minister, the other members of E and E(EA), and Sir Robert Armstrong.

*Yours sincerely,*

*Nicholas Mclines*

JOHN NOTT

(Approved by the Secretary of State and signed in his absence.)