

HC(81) 33rd
Conclusions

COPY NO 79

CABINET

CONCLUSIONS of a Meeting of the Cabinet
held at 10 Downing Street on
TUESDAY 20 OCTOBER 1981
at 10.00 am

PRESENT

The Rt Hon Margaret Thatcher MP
Prime Minister

The Rt Hon William Whitelaw MP
Secretary of State for the Home Department

The Rt Hon Lord Carrington
Secretary of State for Foreign and
Commonwealth Affairs

The Rt Hon Sir Geoffrey Howe QC MP
Chancellor of the Exchequer

The Rt Hon Sir Keith Joseph MP
Secretary of State for Education and Science

The Rt Hon Francis Pym MP
Lord President of the Council

The Rt Hon James Prior MP
Secretary of State for Northern Ireland

The Rt Hon Peter Walker MP
Minister of Agriculture, Fisheries and Food

The Rt Hon Michael Heseltine MP
Secretary of State for the Environment

The Rt Hon George Younger MP
Secretary of State for Scotland

The Rt Hon Nicholas Edwards MP
Secretary of State for Wales

The Rt Hon Humphrey Atkins MP
Lord Privy Seal

The Rt Hon Patrick Jenkin MP
Secretary of State for Industry

The Rt Hon John Biffen MP
Secretary of State for Trade

The Rt Hon David Howell MP
Secretary of State for Transport

The Rt Hon Norman Fowler MP
Secretary of State for Social Services

The Rt Hon Leon Brittan QC MP
Chief Secretary, Treasury

The Rt Hon Baroness Young
Chancellor of the Duchy of Lancaster

The Rt Hon Nigel Lawson MP
Secretary of State for Energy

SECRET

THE FOLLOWING WERE ALSO PRESENT

The Rt Hon Cecil Parkinson MP
Paymaster General

The Rt Hon Michael Jopling MP
Parliamentary Secretary, Treasury

SECRETARIAT

Sir Robert Armstrong
Mr R L Wade-Gery (Items 3 and 4)
Mr P L Gregson (Item 5)
Mr D M Elliott (Items 3 and 4)
Mr D J L Moore (Item 5)
Mr D H J Hilary (Items 1 and 2)
Mr L J Harris (Items 1 and 2)

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PARLIAMENTARY
AFFAIRS

1. The Cabinet were informed of the business to be taken in the House of Commons during the following week.

THE HOME SECRETARY said that it was unlikely that the Government would succeed in any attempt to delete in the House of Commons the new clause on Gibraltar inserted in the British Nationality Bill by the House of Lords. Even if the Commons were to disagree the new clause, it was likely that it would subsequently be reinstated by the House of Lords. After discussing the matter with the Prime Minister and the Chief Whip, he had come to the conclusion that the Government should not seek to reverse the Lords' decision. The consequent difference in treatment between Gibraltar and Hong Kong would cause some resentment in Hong Kong, but should not create undue difficulties.

The Cabinet -

Took note.

INDUSTRIAL
AFFAIRS

British Leyland

Previous

reference:

(80) 16th

conclusions,

page 4

2. THE SECRETARY OF STATE FOR INDUSTRY said that at the end of the previous week the British Leyland workforce had voted by a large majority in favour of strike action from 1 November in pursuit of their pay claim, and the situation was extremely delicate. The Chairman of the company, Sir Michael Edwardes, had made it clear that, if the strike went ahead, the Board would not be able to continue with the strategy contained in its corporate plan, and that immediate steps would have to be taken to dispose of at least some, and possibly all, of the company's assets; letters would be sent on 3 November to those on strike, saying that they had in effect dismissed themselves and were no longer employed by the company. He would appear on television in the course of the following week to explain the consequences of the proposed strike for British Leyland and its suppliers, and to make it clear that he remained open to further approaches from the unions concerned at any time. The unions had so far made no attempt to renegotiate the existing productivity agreements which had been heavily criticised by some sections of the workforce. There was room for some flexibility by the company in this area. The handling of the negotiations, as he himself had repeatedly made clear, was entirely a matter for the company. He would remain in contact with Sir Michael Edwardes, and would consider circulating a memorandum to the Ministerial Committee on Economic Strategy setting out the likely economic and industrial consequences if British Leyland were effectively to be liquidated.

THE PRIME MINISTER, summing up this part of the discussion, said that although there was no objection to the Secretary of State for Industry remaining in informal contact with Sir Michael Edwardes, there could be no question of the Government interfering in the industrial relations of the company, and the Chairman had the Government's full support in the line which he was pursuing.

employment

THE SECRETARY OF STATE FOR EMPLOYMENT said that the latest unemployment statistics would be published later that day. The figures, which were still distorted by the effects of the Civil Service industrial action, were more than usually difficult to interpret. The crude figures showed a fall in unemployment of some 10,000 but the seasonally adjusted figures, though still below 3 million, suggested some acceleration of the rate of increase. On the positive side, vacancies had increased by 2,000, with overtime up and short-time working down.

The Cabinet -

Took note.

FOREIGN
AFFAIRS

Canada

previous

reference:

(81) 31st

conclusions,

minute 1

3. THE FOREIGN AND COMMONWEALTH SECRETARY said that the Canadian Prime Minister, Mr Trudeau, was now talking of a substantial compromise between the Federal Government and the eight dissident Provincial Governments over the proposed legislation to patriate the Canadian Constitution, but the possibility of such a compromise remained uncertain and there was a real danger of the Canadian Government's proposals reaching Westminster in substantially their present form. This would not now happen before early November. Meanwhile the British Government's proposed reply to the report on the subject by the Foreign Affairs Committee of the House of Commons had been revised to take account of the judgment which the Canadian Supreme Court had delivered in September; but this reply would not be published until after proceedings in the Canadian Parliament had been concluded.

In the course of a brief discussion it was noted that the Canadian Supreme Court's judgment had increased the likelihood of the British Parliament rejecting the Canadian proposals, on the grounds that, if Ottawa had overridden one constitutional convention, Westminster could not reasonably be regarded as bound by another. If this happened, Britain would be accused of interfering in Canadian affairs and Anglo-Canadian relations could be severely damaged. Further thought would need to be given to what course the British Government should follow if the Canadian Bill were defeated at Westminster. Simple patriation of the Constitution, with the amending formula but without the Bill of Rights proposed by the Canadian Government, might then be the best course; but this would be open to the objection that it would breach the convention that Britain was not entitled to legislate on Canadian affairs except in accordance with a Canadian request.

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THE FOREIGN AND COMMONWEALTH SECRETARY said that the victory of Mr Andreas Papandreou's Socialist Party in the Greek general election was a disturbing development, although some of its international effects might prove less serious than had been feared. His plan to hold a referendum on Greece's membership of the European Community required the agreement of the President, Mr Karamanlis, which was unlikely to be forthcoming. He could, however, be expected to seek a renegotiation of the terms of Greek membership, and while this was in progress there would be a danger of Greece proving an obstructive and unhelpful partner in the Community. It was unlikely that Mr Papandreou would seek to take Greece out of the North Atlantic Alliance. But he might well leave the military structure of the North Atlantic Treaty Organisation.

THE FOREIGN AND COMMONWEALTH SECRETARY said that the change of leadership in Poland was probably for the better, and might lead to a Government which was more dynamic and better able to take decisions. The new Party leader, General Jaruzelski was essentially a moderate. The leader of the Solidarity trades union movement, Mr Walesa, had welcomed his appointment.

THE FOREIGN AND COMMONWEALTH SECRETARY said that the planned Marylebone Cricket Club tour of India was now unlikely to take place, since the Indians were refusing on political grounds to accept two members of the British team who were said to have had sporting links with South Africa. It had been suggested that their presence might have led to public disorder at cricket matches in which they took part. In view of Britain's many interests at stake in India, and not least the steel contract on which the Lord Privy Seal had reported to the Cabinet on 24 September, it would be important for members of the Government to avoid public comment on the issue as far as possible. Where comment was unavoidable, the essential point to make was that Britain stood by and complied with the Commonwealth's Gleneagles Agreement on sporting contacts with South Africa; if necessary it could be added that the Government were not prepared to put pressure on individual sportsmen.

THE FOREIGN AND COMMONWEALTH SECRETARY said that, although no decision had yet been taken, it now seemed probable that small-scale British participation in the proposed Sinai Multinational Force would be essential in order to avoid the danger of Israel refusing to hand back the rest of the Sinai to Egypt on the due date in the spring of 1982. From Britain's point of view a balance of disadvantages was involved. If participation could not be avoided, every effort would

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need to be made to discourage other Arab states from penalising British interests. Meanwhile a series of mischances had prevented Britain from being represented at General Dayan's funeral in Israel either by the Parliamentary Under Secretary, Foreign and Commonwealth Office, Lord Trefgarne, as originally intended, or by Her Majesty's Ambassador in Tel Aviv.

THE FOREIGN AND COMMONWEALTH SECRETARY said that the Prime Minister and he would be attending the Summit Meeting between developed and developing countries in Mexico on 22-23 October. Although international expectations were high, nothing concrete was in fact likely to result.

The Cabinet -

Took note.

4. THE FOREIGN AND COMMONWEALTH SECRETARY said that the French Government had now published a memorandum containing their proposals for the "relance" of the Community. It was something of a damp squib, consisting largely of a collation of relatively minor individual proposals for the practical development of Community policies. Many aspects of the memorandum accorded well with United Kingdom views, though (eg the proposal for a 35-hour working week) were not acceptable. In general the memorandum should not cause the United Kingdom any embarrassment, provided that it could be handled separately from the mandate negotiations.

THE CHANCELLOR OF THE EXCHEQUER said that the orientation debate on the mandate which had taken place at the meeting of the Council of Ministers (Economic and Finance) on 19 October had shown some signs of advance towards United Kingdom objectives. The atmosphere had been less hostile than at the start of the budget restructuring negotiations. The Dutch had spoken in terms which echoed his own Hague speech, and the Germans had made clear their inability to accept any longer a situation in which two member states bore the whole burden of net contributions to the Community budget. It would be crucial to British aims to keep the Germans pressing for a general solution rather than pursuing relief for themselves alone. The discussion on the non-life insurance services Directive had been disappointing, in that a number of member states who had earlier given general assurances of support had retreated from these positions. It would be necessary to push even harder if there were to be any progress on this Directive during the United Kingdom Presidency.

October Council
Agriculture
Ministers

THE MINISTER OF AGRICULTURE, FISHERIES AND FOOD said that an orientation debate on the mandate had also taken place at the meeting of the Council of Ministers (Agriculture) on 19 October. Only the United Kingdom, and to a lesser extent the Netherlands, had pressed for reform of the Common Agricultural Policy and constraints on its budgetary cost. Most other member states had stressed the need to protect farm incomes, and Herr Ertl, the German Minister, had made an unhelpful intervention.

Previous
reference:
C(81) 31st
conclusions,
minute 2

Common
Fisheries Policy

THE MINISTER OF AGRICULTURE, FISHERIES AND FOOD said that, following the successful negotiation of a mini-package at the 29 September Council of Ministers (Fisheries), the Council would meet again on 26 October. This was unlikely to make much progress; the crucial negotiations would take place in November, when there was still some chance of getting agreement on a revised Common Fisheries Policy.

Previous
reference:
C(81) 31st
conclusions,
minute 2

The Cabinet -

Took note.

ECONOMIC
POLICY AND
PUBLIC
EXPENDITURE

5. The Cabinet considered a memorandum by the Chancellor of the Exchequer (C(81) 50) on economic policy and public expenditure and a memorandum by the Chief Secretary, Treasury (C(81) 51), making specific proposals for individual public expenditure programmes.

Previous
reference:
C(81) 32nd
conclusions,
minute 4

The Cabinet -

1. Agreed that the aim, in further discussions of public expenditure programmes, should be to arrive at public expenditure planning totals as near as possible to those of £113.5 billion in 1982-83 and of £118.1 billion in 1983-84 proposed by the Chancellor of the Exchequer and the Chief Secretary, Treasury, in C(81) 50 and 51.

2. Agreed that, where appropriate, there should be further bilateral discussion between the Chief Secretary, Treasury, and the Minister concerned.

3. Took note that in other cases, except for certain specific matters which were to be discussed in the Ministerial Committee on Economic Strategy or other fora, the Prime Minister would arrange for discussion by a small group of Ministers under the chairmanship of the Home Secretary which would make recommendations to the Cabinet.

Cabinet Office

20 October 1981

CABINET

LIMITED CIRCULATION ANNEX

CC(81) 33rd Conclusions, Minute 5

Tuesday 20 October 1981 at 10.00 am

ECONOMIC POLICY
AND PUBLIC
EXPENDITURE

Previous

reference:

CC(81) 32nd

conclusions,

minute 4

The Cabinet considered a memorandum by the Chancellor of the Exchequer (C(81) 50) on economic policy and public expenditure and a memorandum by the Chief Secretary, Treasury, (C(81) 51) making specific proposals for individual public expenditure programmes.

THE CHANCELLOR OF THE EXCHEQUER said that his memorandum set out the factors relevant to decisions about public expenditure in 1982-83 and later years and to decisions which he would take at the time of his next Budget on taxation and the Public Sector Borrowing Requirement (PSBR). The immediate economic prospects were for a slower improvement than had been hoped, with inflation coming down more slowly than expected, and unemployment remaining disturbingly high. There were, however, encouraging signs on output and the longer term prospects gave ground for guarded optimism. It was a delusion to think that any alternative economic strategy would, within the lifetime of the present Parliament, lead to any substantially better outturn. There was no easy solution by way of financing more expenditure by either more borrowing or more taxation. The Treasury had estimated that additional spending on Government purchases that raised the PSBR by £1 billion in 1982-83 could reduce unemployment by 50,000 by the end of 1983 but would be likely to lead to increases in interest rates and a worsening in the prospect for inflation; and the gains to output and employment would be eliminated by the end of 1985. Against this background, he recommended that the Government should plan for a PSBR for 1982-83 not greater than the £9 billion foreseen at the time of the 1981 Budget. This was not a precise figure, nor did it represent the outcome of the application of any particular economic theory: it represented a practical judgment of what it might be possible to borrow in the financial markets at reasonable levels of interest rates. Anything higher than this could lead to increases in interest rates and add to the problems, already evident, of funding the PSBR. As it was, debt service costs this year would be in the order of £15 billion: higher than most public expenditure programmes. He further recommended against any increases in the real burden of taxation, which was already too high. His present forecast already assumed

that, in the 1982 Budget, income tax thresholds would be raised in line with inflation (under the Rooker-Wise provisions), as would excise duties; and that National Insurance Contributions would rise to balance the National Insurance Fund. He and the Chief Secretary, Treasury, recognised that the pressures on Departmental Ministers for additional expenditure were such that it would not realistically be possible to hold public expenditure totals to the provision in the last Public Expenditure White Paper (Cmnd 8175) of £109.9 billion in 1982-83 and £113.9 billion in 1983-84; they were recommending that the planning totals for public expenditure should be £113.5 billion in 1982-83 and £118.1 billion in 1983-84. These totals were the maximum which could be afforded if there were not to be real increases in taxes in the 1982 Budget on top of the revalorisation already in prospect. Even if these totals were achieved, it would be impossible for him to make any reductions in the National Insurance Surcharge or any real increases in tax thresholds in his next Budget. The implications for tax changes in 1983 and 1984 were necessarily less certain but, while he could not yet count on it, his aim would be to take fiscal action in those years to assist further in the reduction of inflation and the improvement of efficiency and competitiveness in British industry.

In discussion the following were the main points made:-

- a. Most Ministers agreed that it was right to aim for a PSBR of the order of £9 billion in 1982-83, provided that the figure was not regarded as sacrosanct. Some commentators were expecting a higher figure and this, together with the great uncertainty inherent in forecasting the PSBR, suggested that it might be reasonable to accept something higher if further discussion of the public expenditure and taxation options pointed to that. On the other hand, there would be risks in planning now for anything higher than £9 billion; the forecast already incorporated a number of assumptions which could well prove to be optimistic.
- b. It was essential that the expenditure and taxation decisions should give a psychological lift to the morale of private industry. This had been low since the measures taken in the 1981 Budget; industry felt that, apart from the measures taken to help small businesses, the Government had not done enough to meet its objectives of stimulating wealth creation. In particular the National Insurance Surcharge was seen as a tax on employment and as a major disincentive imposed by the Government on the private sector.

c. In discussions earlier in the year of public expenditure the Cabinet had agreed that it would be desirable to increase the proportion of capital expenditure in the total. It was, therefore, particularly disappointing that the Chief Secretary, Treasury's, paper showed that, if his proposals were to be accepted, central and local Government capital expenditure would fall in 1982-83 to 9.5 per cent of total expenditure, excluding the nationalised industries, compared with 10.2 per cent in the last Public Expenditure White Paper. Such cuts would have damaging repercussions on employment and activity by private sector firms. In some cases small cuts in capital grants could lead to the collapse of firms producing machinery and equipment; in others the projects which might be cut were likely to give a sound economic return. On the other hand, as the Chief Secretary, Treasury, pointed out, only about 5 per cent of the additional expenditure bids put forward by Departments were for capital expenditure. In practice, any substantial increases in capital expenditure within the present proposed totals could be financed only by further cuts in the Social Security programme. The Cabinet had not been persuaded, in earlier discussions, that it would be realistic to call for a general limitation on pay increases to a very low figure, coupled with abatement in the indexation of benefits, in return for increased capital expenditure on investment which would promote the revival of the economy and a reduction of unemployment.

d. There should be greater readiness to encourage private sector financing of public sector capital projects. Provided that the private sector genuinely bore the risks, borrowing for such investment should not count against the PSBR; this should be practicable for such profitable nationalised industries as British Telecommunications. On the other hand, it had been disappointing that most of the proposals so far made were for private sector borrowing backed by Government guarantee. Such borrowing left the risks with the Government and cost more than borrowing through the National Loans Fund.

e. There would be considerable difficulties in implementing some of the proposals by the Chief Secretary, Treasury for cutting some public expenditure and reducing, or rejecting, additional bids which Departmental Ministers had thought necessary to put forward. In further discussion of these proposals it would be essential to recognise pledges which the Government had already made. Proposals for changes should be socially defensible, maintaining the reputation of the Conservative Party as a caring Party and avoiding any charge of implementing socially divisive policies bearing more

harshly on the poorer members of the community; this was relevant, for example, to the proposals relating to health and social benefits and to council house rents. The implementation of some proposals would require Parliamentary approval and it would be important to avoid proposing measures which might be rejected by Parliament.

f. Some Ministers thought that taxation should be increased above the levels assumed by the Chancellor of the Exchequer in his memorandum if that were necessary to finance additional public expenditure at the margin. It would certainly be very difficult to defend the avoidance of real tax increases for the better-off if at the same time some Social Security benefits were not to be fully indexed. On the other hand, it could well prove very difficult to secure Parliamentary acceptance of the revalorisation of indirect taxes and of the increases in the National Insurance contribution, which the Chancellor of the Exchequer was already planning. It would be particularly difficult to secure Parliamentary approval yet again to less than full indexation of income tax thresholds. Any real increases in income tax paid by managers would be severely criticised. Increases in capital taxation could not be expected to yield large amounts of revenue.

g. Some Ministers were sceptical of the assessment, in Annex B of C(81) 50, of the implications for public finances of additional public expenditure on manpower. The analysis suggested a cost per job of £20,000 and this seemed implausibly high. There were other measures which could be introduced at a much lower cost per job: for example, certain special employment measures and the use of small amounts of public funds, or guarantees, to stimulate significant private sector investment and employment.

THE PRIME MINISTER, summing up the discussion, said that the Cabinet recognised the dangers of planning for increases in the PSBR which would then lead to problems of funding and to increases in interest rates which would themselves be damaging to industry. While some members of Cabinet would not rule out the possibility of real increases in taxation, there was already a likelihood of very considerable difficulties in winning Parliamentary acceptance of the revalorisation of indirect taxes and the increases in the National Insurance Contributions, which the Chancellor of the Exchequer was assuming in his planning. This pointed to looking, in further discussion of individual public expenditure programmes, for overall planning totals as near as possible to those proposed by the Chancellor of the Exchequer and the Chief Secretary, Treasury. In this further discussion it would be necessary to have regard :

to the political impact of the changes proposed and to the likelihood of their acceptability in Parliament. Some programmes might be discussed further bilaterally between the Chief Secretary, Treasury and the Minister concerned. Plans had already been made for the Ministerial Committee on Economic Strategy to discuss proposals on employment and training measures and on regional development grants. She would arrange for other programmes to be examined, prior to further discussion by the Cabinet, by a small group of Ministers under the chairmanship of the Home Secretary. In the meantime it was essential to preserve the confidentiality of the Cabinet's discussions, and to avoid any misleading and premature publicity which could be damaging to confidence in the financial markets. She would if necessary indicate in Parliament that the Cabinet had held one of a series of meetings on public expenditure which were aimed not at cuts but at holding increases within limits which the country could afford.

The Cabinet -

1. Agreed that their aim, in further discussions of public expenditure programmes, should be to arrive at public expenditure planning totals as near as possible to those of £113.5 billion in 1982-83 and of £118.1 billion in 1983-84 proposed by the Chancellor of the Exchequer and the Chief Secretary, Treasury in C(81) 50 and 51.
2. Agreed that, where appropriate, there should be further bilateral discussion between the Chief Secretary, Treasury and the Minister concerned.
3. Took note that in other cases, except for certain specific matters which were to be discussed in the Ministerial Committee on Economic Strategy or other fora, the Prime Minister would arrange for discussion by a small group of Ministers under the chairmanship of the Home Secretary which would make recommendations to the Cabinet.

Cabinet Office

21 October 1981