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SECRET

Prime Minister



These assumptions are to be published on a date to be fixed before the end of November.

Their effect on the current pay round is likely to be adverse and I suggest

Treasury Chambers, Parliament Street, SW1P 3AG

01-233 3000

that we ask that consideration be given

given

to the impact on current pay negotiations (mineworkers, waterworkers).

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but this will be inconsistent with the rest of the forecast and will strain credibility. See also Alan Walters' note. Content to agree with

PRIME MINISTER

ECONOMIC ASSUMPTIONS

As you know, towards the end of next month we have to publish Chancellor's (i) the forecast required by the Industry Act (IAF) and (ii) the conclusion? report by the Government Actuary (GA) on the National Insurance Fund. So once again we have to decide on the economic assumptions that we give the GA; they will, of course, be published in his report.

MS 30/10

2. The assumptions to be provided are those in relation to unemployment in 1982-83, earnings for 1982-83, and the inflation between the fourth Quarter of 1981 and the fourth Quarter of 1982. The purpose of this minute is to let you know what I propose to have published, in the light of the latest forecasts available to me, and the need to produce figures which are both credible and - in the case of prices and earnings - helpful in their influence on expectations.

3. On unemployment I propose that we should publish, as an average level for 1982-83, a figure of 2.9 million on the narrow definition - that is, excluding school leavers, adult students and the temporarily stopped. These groups are forecast at 225,000, making a total of 3.1 million on a wide definition. These figures are for Great Britain; the United Kingdom figure (i.e. including Northern Ireland) is about 100,000 more than this, but this figure does not have to be given.

4. Obviously, we should prefer to avoid publishing, as a Government forecast, a figure of over 3 million. But in fact it is relatively conservative - and might, by now, be so regarded.

SECRET

Handwritten notes: ce A Duguid, J Vercher Vercher's, share John, can we not force, Treasury Chambers, PRIME MINISTER, ECONOMIC ASSUMPTIONS, to timing, insofar as this is practical, John Vercher suggests a lower figure - 6 1/2% for earnings, but this will be inconsistent with the rest of the forecast and will strain credibility. See also Alan Walters' note. Content to agree with

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On the narrow definition unemployment now stands at 2.63 million seasonally adjusted. The increase over the last few months has averaged 50,000 per month. At this rate the figure is likely to rise to 2.9 million as 1982-83 begins, so to use this figure as the average for the year implies a considerable slowing down in the rate of increase. I do not think we could sensibly or justifiably publish a lower figure.

5. For prices, I propose a figure of 10 per cent as the increase in the RPI between November 1981 and November 1982. This is at the bottom end of the range of figures given by our present forecast. But I think it is justifiable to go for this lower number. On the other hand I do not think it would be feasible to go for a number as low as 9 per cent and still retain credibility, having regard to the fact that the year-on-year figure is currently 11.4 per cent, and the figure for November (published in December) will probably get to 12 per cent or more having regard to increases such as the rise in mortgage interest which are in the pipeline. 10 per cent is consistent with our view that there has been a pause in the deceleration of inflation, but that we should be able to get to single figures by early 1983. It is also consistent with the 9 per cent factor being used for non-pay elements in public expenditure plans.

6. For earnings I propose a figure of 7½ per cent. This will be consistent with settlements of about 5 per cent on average, coupled with drift and increased overtime working to be expected in line with our projections of improvement in output. Taken with the prices figure it implies a fall in real earnings of about 2½ per cent over the year. The figure for earnings gives a good deal of weight to our expectations of a substantially lower level of wage settlement.

7. In arriving at these figures I have - as explained above - tried to balance the need to influence expectations so far as we can against the need for credibility. I believe that the balance



is right, and accordingly propose to arrange for these figures to be published in the GA's report and/or IAF as appropriate.

8. Looking ahead, we shall as usual shortly have to take decisions about any changes in National Insurance Contributions, and also on allied matters including the National Insurance Surcharge, which would take effect from next April. There is a complex network of issues here which I shall be discussing in the near future with the Secretary of State for Social Services. It is too early to say what we shall propose. But I should let you know that I think our general approach should be governed by two considerations; first, to spare employers as far as possible from increases in their burden, leaving the weight of the increases to rest on employees; and second, to maximise the help we can get for the 1982-83 PSBR through the NIC machinery, so as to increase our flexibility of manoeuvre in the next Budget. This is, of course, broadly the approach we took last year. I should add that my preliminary examination shows that, on most of the options we might adopt, primary legislation would be necessary before the end of January, and this is a factor which we shall have to take into account.

9. I am copying this to the Secretary of State for Social Services and to Sir Robert Armstrong.

A handwritten signature in black ink, appearing to be 'G.H.'.

(G.H.)

27 October 1981