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PRIME MINISTER

PUBLIC EXPENDITURE

I attach the first draft of my report on public expenditure. This shows the progress made in reaching agreement both in bilaterals between the Chief Secretary and the spending Ministers and in my Ministerial Group (M.I.S.C. 62). It also identifies the issues which remain to be resolved. The purpose of this minute is to give you early advice on how things now stand so that you have an opportunity of holding meetings yourself to try and settle some at least of the outstanding issues before the report is circulated to the Cabinet.

A large number of programmes have now been agreed i.e. Industry (except for Regional Development Grants), Energy, Trade, E.C.G.D., Employment, Transport, Home Office, Education and Science, Arts and Libraries, Forestry Commission, Scotland, Wales and Northern Ireland and the External Financing Limits for all the nationalised industries. (I should of course point out that some of these programmes will be affected by our decisions on local authority current expenditure, and that the programmes for Scotland, Wales and Northern Ireland will be affected consequentially by outstanding decisions on some other programmes.)

As a result of the agreements on these programmes it is already clear that the public expenditure totals will be higher than those proposed by the Chancellor of the Exchequer and the Chief Secretary in C(81)50 and 51. Even assuming the lowest outcome for the programmes not yet agreed, the totals are increased by some £800 million in 1982/83 and the succeeding years. Certain of the proposals already agreed (e.g. on student grants, the "Christmas Bonus" for pensioners, the earnings rule for pensioners and prescription charges) are politically sensitive and this is brought out in the draft report.

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Leaving aside those matters which are under separate collective discussion (i.e. Regional Development Grants, and the two major and related issues of local authority current expenditure and housing) the remaining programmes which have to be settled are:

Defence;  
F.C.O. (including O.D.A.);  
Agriculture;  
Other Environmental Services and P.S.A.;  
Health;  
Social Security.

My comments on these outstanding programmes are as follows:

a. Defence

We tried hard in M.I.S.C. 62 to reach agreement but, as you will have seen from the Secretary of State for Defence's minute to me of 3rd November and the Chief Secretary's response of 9th November, we have not been able to arrive at a solution. The sums at stake are £125 million in 1981/82, £374 million in 1982/83, £597 million in 1983/4 and £895 million in 1984/85.

b. F.C.O. (including O.D.A.)

The Foreign and Commonwealth Secretary sees great difficulty in making the savings proposed, and especially a cut of about £50 million a year in overseas aid. There is also an additional bid of £60 million in 1982/83 for aid to Poland which is under discussion in the OD Committee. The sums at stake overall are £128 million in 1982/83, £72 million in 1983/84 and £74 million in 1984/85.

c. M.A.F.F./I.B.A.P.

There is a major difference of view over capital grants; the Minister of Agriculture wants to increase them, mainly for the

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benefit of producers of agricultural equipment, but the Chief Secretary is seeking a reduction in either rates of grant or coverage. The Chief Secretary was prepared to make various concessions on the agricultural programmes (notably on hill livestock compensatory allowances and on the beef premium scheme) if the Minister would be prepared to agree to a small reduction in capital grants. Agreement could not be reached, and the Chief Secretary's offers therefore lapsed. The sums at stake on both programmes taken together are £93 million in 1982/83, £149 million in 1983/84 and £133 million in 1984/85.

d. Other Environmental Services and P.S.A.

On "other environmental services" the Chief Secretary proposed savings of £120 million in 1982/83 and £165 million in each of the later years. The Secretary of State for the Environment was willing to agree only to savings of £10 million in 1982/83 and £15 million in each of the later years. He accepted that the cuts proposed could be achieved but he thought it wrong in principle to reduce capital expenditure by local authorities and water authorities. M.I.S.C. 62 will however recommend that the Chief Secretary's proposed cuts should be made. So far as the P.S.A. is concerned, the Chief Secretary proposed a saving of £20 million a year over the period. The Secretary of State for the Environment agreed with M.I.S.C. 62 that this saving could be made but wanted other Ministers to realise that their programmes would inevitably be affected; this is being made clear in the report.

e. Health

There are major political issues relating to the level of expenditure on the hospital service, increases in existing health charges, and the introduction of new charges. Although there was a convergence of views between the Chief Secretary and the Secretary of State for Social Services on certain matters, we were unable to secure an overall agreement. M.I.S.C. 62 considered that it would be impracticable, mainly because of

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public commitments, to implement all the proposals for new charges. The sums at stake for the programme as a whole are £240 million in 1982/83, £427 million in 1983/84 and £543 million in 1984/85.

f. Social Security

This is by far the largest programme and one which is very sensitive politically. Although agreement has already been reached between the Chief Secretary and the Secretary of State for Social Services on some difficult issues referred to in paragraph 3 above, there are some major unresolved issues relating to the uprating of benefits not subject to an absolute pledge of price protection. These are set out more fully in the draft report; the sums at stake are £191 million in 1982/83, £562 million in 1983/84 and £589 million in 1984/85.

I am sure that we should make every effort to reach some accommodation on Defence and Overseas Aid before the Cabinet resumes its discussion on public expenditure. You may also feel that it is worthwhile to try and make more progress on some of the other outstanding programmes. I fear however that we have gone as far as we can in bilateral discussion and in M.I.S.C. 62. I hope that you will be willing to chair some informal meetings yourself with the relevant spending Ministers and the Chief Secretary. If you felt that it would be helpful for me to take part in any of these meetings, I should of course be ready to do so.

I am sending copies of this minute to the Chancellor of the Exchequer, the Secretaries of State for Scotland and for Industry, the Chief Secretary, Treasury, the Chief Whip and Sir Robert Armstrong.

L.W.

11 November, 1981

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