SECRET AND PERSONAL

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PRIME MINISTER

PUBLIC EXPENDITURE IN 1983-84

Following our talk at Chequers on Saturday, I have prepared the attached paper for circulation to Cabinet colleagues tomorrow morning in the new restricted CMO series. As agreed, the key proposals now are for a 2 per cent reduction in non-pay cash limits, and a 1 per cent reduction in the pay limits, together with the introduction of the end-year flexibility scheme. Please let me know if you would like any further changes.

2. Peter Middleton proposes to brief key Permanent Secretaries on Wednesday morning. I think that this would be useful; though it obviously does not remove the need for me to see a number of colleagues privately before Thursday.

3. The right time to announce these decisions, assuming they go through, would I think be at Question Time on Thursday afternoon, when it is the Treasury's turn. I should like to avoid making a Statement as such, but I plan to talk to John Biffen about this tomorrow.

NL.

N.L.
4 July 1983

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5 July 1983

V. like to take ~~a decision today~~

CABINET

PUBLIC EXPENDITURE IN 1983-84

Memorandum by the Chancellor of the Exchequer

Overall, public expenditure this year is running substantially ahead of the figures agreed by Cabinet and published in the February White Paper (Cmnd 8789). If we do nothing int rates will rise. Unless we take steps will abort the recovery & prospects for jobs.

2. The surge in expenditure which began late in 1982-83 has continued unabated. Demand related programmes - particularly agricultural support and social security benefits - are growing very rapidly. Local authority current expenditure and nationalised industry borrowing are also likely to be higher than envisaged. The EC Budget refund agreed at Stuttgart was £300 million lower than the White Paper figure. In the light of the 1982-83 outturn, we are also expecting some £600 million less shortfall - about £300 million of it on defence votes, and the rest spread across the field - in cash limited expenditure than the £1200 million which was assumed in the White Paper.

3. The rapid growth in expenditure is reflected in very high rates of public borrowing so far this year. The monthly figures for central government borrowing have caused concern in the markets, and the quarterly figures to be published this month are likely to increase it. The first quarter CGBR figure, due on 11 July, is likely to be some £5,400 million, which is £2,000 million more than the comparable figure last year, and very nearly half the figure envisaged at Budget time for the year as a whole. If it were thought that we were willing to see expenditure and borrowing on this scale continue ~~unchecked,~~ first confidence would suffer, and interest rates would rise ~~be pushed up,~~ damaging the private sector and the prospects for recovery.

4. We must not allow this to happen. We need to do what we can to step up the disposals programme; and this is already in hand. But that alone will not be sufficient. We also need to tackle the spending surge at source, and bring this year's expenditure totals closer to the Cmnd 8789 path.

5. I emphasise that I am not asking for cuts in published expenditure totals this year: the aim is simply to get back closer to the White Paper totals. It makes sense to consider the problem immediately in order to give the maximum amount of time in which to make the necessary adjustments.

6. The first and most obvious step is to try to curb the increases on non-cash-limited demand-determined expenditure. I should be grateful if those colleagues concerned would explore all appropriate available options.

7. Realistically, however, we cannot expect to achieve a great deal by that route. To get back on course we shall have to take action on cash limits.

8. I believe (There is ~~in fact~~ some room for such action, (particularly on the non-pay side,) because prices this year are in general rising ~~slower~~ more slowly than was ~~expected~~ estimated when departments drew up their plans. On the pay side we need to take account of the pressure resulting from our decision earlier in the year to finance the non-industrial civil service pay increase from the original provision.

Subst. Robin's section

9. I therefore propose a reduction of 1 per cent on the 'pay' element and of 2 per cent on the non-pay element of all central government cash limits. The 'pay' element would include general administrative expenditure (gae). I propose excluding Rate Support Grant, because it is very doubtful whether cuts would actually lead Local Authorities to reduce their current expenditure, and Local Authority capital expenditure.

10. It would not be right to exempt the nationalised industry External Financing Limits, for nationalised industry borrowing is a substantial component of the current surge. I therefore propose a 2 per cent cut in the provision for total EFLs, to be allocated in proportion to turn-over.

11. If Cabinet agrees, the Treasury will agree with Departments a detailed list of the cash limits affected. The savings would be in the range £650-£700 million gross, or around £500 million net of some further reduction in shortfall.

12. At the same time, and to discourage a repetition of last year's end-year surge, I also propose to introduce a scheme of end-year flexibility as outlined by the previous Chief Secretary in C(82)29. (Individual Local Authorities already have a measure of end-year flexibility, and so would not be included.) There would be considerable managerial advantage in such a scheme, and spending Departments have been pressing for it. It would mean that spending in this financial year would be reduced, by perhaps a further £100 million (though pressure next year would of course be increased).

13. The present problem arises in part because it has proved so difficult to provide reliable forecasts of rates of spending. This is a problem throughout the year, but it especially acute towards the year-end, as Departments seek to spend up to their cash limits. There have also been severe problems over forecasting demand-related expenditure. I therefore seek the co-operation of spending Ministers in improving the financial information flows from their departments to the Treasury during and particularly at the end of the financial year. Detailed proposals will be made at official level shortly.

in order to get closer to the Public Expenditure published totals

14. To sum up, I propose:-

a. consideration by the Departments concerned of possible ways of slowing the increase in demand-determined non-cash limited spending;

b. a reduction of 2 per cent in the non-pay element of central government cash limits - to yield around £350 million in 1983-84;

c. a reduction of 1 per cent in the pay (and gae) elements, yielding perhaps £100 million net;

d. a reduction of 2 per cent in nationalised industry EFLs, allocated in proportion to turn-over;

e. the introduction of a scheme of end-year flexibility on central government capital expenditure at the end of 1983-84, which should take the saving this year to around £600 million;

f. that all spending Ministers should cooperate in improving information flows to the Treasury about the course of expenditure during the year.

NL.

N L

HM Treasury
5 July 1983

PUBLIC EXPENDITURE

It is now clear that public expenditure is running at a significantly higher level than is consistent with the 1983-84 planning total of £119.6 billion announced in the Public Expenditure White Paper (Cmnd 8789) presented by the then Chancellor on 1 February. Some adjustment is clearly needed; and I have therefore decided that immediate action must be taken to bring about savings that will bring total spending closer to the planned path. It is both more efficient in terms of departmental management of programmes, and more effective, to take this action straightaway.

2. Accordingly, the cash limits for the current year will be reduced. The effect ~~of the reduction~~ will be a 1 per cent ~~cut~~ reduction in respect of the pay and central government administrative element, and a 2 per cent ~~cut for~~ reduction in the remainder. The new cash limit figures will be announced as soon as possible.

3. The total provision for the External Financing Limits of the nationalised industries will similarly be reduced by 2 per cent. This reduction will be allocated in proportion to their turnover.

4. The effect of these measures will be to remove at least £500 million of over-~~shoot~~ spending beyond the planned ~~spending~~ total.

5. In addition, the programme of asset sales during the current year will be increased by a further £500 million.

6. Finally, I am also taking the opportunity to introduce some improvements in expenditure control. In particular, a scheme of end-year cash limits flexibility will be introduced. This will permit some carry-forward of underspend on central Government capital programmes. Such a change has of course long been advocated by departments, such as Defence, with substantial capital programmes involving expenditure stretching over a number of years. The change, I believe, is fully justified on managerial grounds, but introducing it as from this financial year should in

practice, by reducing the end-year surge, reduce expenditure in the current year by some £100 million: the effects in future years will be taken into account in the forthcoming Public Expenditure Survey. I am satisfied that Parliamentary control of expenditure will not be diminished.

7. The overall effect of the savings and other measures which I have announced will be to reduce this year's likely public expenditure outturn by over £1 billion. They do not imply any ~~cuts~~ reductions in the total, as published in the February White Paper: rather they are designed to bring spending closer to the course laid down in my predecessor's White Paper.

8 I told the House on 29 June that, in order to maintain the right balance between public borrowing and interest rates, we intended to maintain firm control of public spending. I also made clear my determination to take action should our objectives be endangered. Our economic strategy has brought

about low inflation and a quickening recovery. We are determined to ensure that unplanned overspending does not deflect our course, and put the recovery at risk.