SECRET

THIS DOCUMENT IS THE PROPERTY OF HER BRITANNIC MAJESTY'S GOVERNMENT

C(83) 21 COPY NO 30

5 July 1983

CABINET

PUBLIC EXPENDITURE IN 1983-84

Memorandum by the Chancellor of the Exchequer

I have to report that overall public expenditure this year is running substantially ahead of the figures agreed by Cabinet and published in the February White Paper (Cmnd 8789).

2. This is reflected in very high rates of public borrowing. 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 central Government borrowing requirement 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, interest rates would rise, damaging the private sector and the prospects for jobs and recovery.

3. 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 total closer to the Cmnd 8789 path.

4. 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. In the light of the 1982-83 outturn, we now expect only half the £1,200 million shortfall in cash-limited expenditure assumed in the White Paper. Of the £600 million extra expenditure now expected, about £300 million is on defence votes, and the rest spread across the field.

5. I emphasise that I am not asking for cuts in the published expenditure total this year: but I am sure that we must get back closer to the White Paper total. To defer action could well mean having to do much more before the autumn, given the likely market reaction to the borrowing figures. And in any case 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.

98

8. I believe that there is in fact some room for such action, particularly on the non-pay side, because prices this year are in general rising more slowly than was expected when Departments drew up their plans. Nor can we exempt the pay side, though 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.

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. 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 (EFLs). For those industries currently forecasting an overrun in their EFLs, remedial action must be taken to ensure that their requirements are kept to the minimum. In addition I propose for the industries overall a 2 per cent cut in the provision for total EFLs, to be allocated in proportion to turnover.

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. This would permit the carry-over of underspends on capital items of up to 5 per cent of the original provision, as described in paragraph 19 of the note attached to C(82) 29. (Individual local authorities already have a measure of end-year flexibility, and I do not therefore propose to include them.) 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 is 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

14. I realise that the proposals in paragraphs 9-11 above will cause some difficulty. But the situation we face is very serious; and the action proposed is the minimum required to hold to our Budget strategy to consolidate the recovery and so improve job prospects. And we must act now.

15. To sum up, in order to get closer to the agreed public expenditure total, I propose:-

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

99

SECRET

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 general administrative expenditure) elements, yielding perhaps £100 million net.

d. A reduction of 2 per cent in nationalised industry EFLs, allocated in proportion to turnover.

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 co-operate in improving information flows to the Treasury about the course of expenditure during the year.

N L

Treasury Chambers

5 July 1983

SECRET

100