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P.0795

PRIME MINISTER

Pay in the coming year
(E(82)53)

BACKGROUND

Although the current pay round (usually regarded as running from August 1981 to August 1982) is not yet over, it seems likely that the final outturn will be reasonably close to the cumulative level of settlements so far. The figures given in the current Department of Employment pay brief (based on a large, but not in all respects completely representative, sample) are as follows:

Private manufacturing: just over 6 per cent
Private non-manufacturing: just over $7\frac{1}{2}$ per cent
Public trading sector: just under $7\frac{1}{2}$ per cent
Public services: just over $6\frac{1}{2}$ per cent
Whole economy: 7 per cent

To these figures must be added an allowance for drift. This may be of the order of 1 or 2 per cent for the whole economy.

2. The figures are lower than those for the 1980-81 pay round, for which the level of settlements in the whole economy was around $8\frac{1}{2}$ per cent, with drift bringing the increase in earnings up to something over 10 per cent. All the major industries in the public trading sector settled lower than in the previous pay round; and the same is true in general of the public services - the only likely exception is the National Health Service. (The industrial civil service and the local government white-collar workers have yet to settle; but they seem likely to do so at around 6 per cent). However, there was a far smaller improvement between pay rounds than there was between 1979-80 and 1980-81: between those two rounds, the rate of increase in earnings fell from over 20 per cent to just over 10 per cent.



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3. Ministers will now wish to consider their approach to the pay round beginning in August 1982. This is the subject of the memorandum by the Chancellor of the Exchequer (E(82)53). The memorandum also refers to the suggestion which has been advanced, mainly by the Secretary of State for the Environment, for a deal with the public sector trade unions under which public investment would be increased in return for pay restraint. A scheme on these lines was discussed in more detail in the minute of 10 May, and the attached note, from the Chancellor of the Exchequer to you. A larger and less well-defined scheme was put forward by the Secretary of State for the Environment in his minute of 27 May; you suggested that this should be discussed by the Committee.

4. The Chancellor of the Exchequer has also circulated a separate memorandum about pay in the public trading sector (E(82)54).

MAIN ISSUES

5. There is hardly likely to be any dissent from the proposition that the Government should aim at a further reduction in the level of pay settlements: that is always desirable, and the larger the reduction, the better. The real questions are how large a reduction it is realistic to aim at; what are the best methods for achieving it; and what are the risks involved?

Size of reduction

6. The Chancellor of the Exchequer suggests that the aim should be a reduction in settlements from 7 per cent to 4 per cent and in the earnings increase from say 8½ or 9 per cent to 6 per cent. This would be a larger reduction in both absolute and percentage terms than was achieved between the 1980-81 and 1981-82 pay rounds: indeed, the reduction in the rate of pay settlements since December 1980 is only of the order of 2 or 3 percentage points. As paragraph 5 of E(82)53 brings out, there are a number of factors in the economic situation which will tend to produce an increase, rather than a decrease, in pay settlements. We understand that the informal monitoring by the Department of Employment suggests that many employers in the private sector are expecting such an increase.

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but without papers and without preparation by officials. MCS

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7. No doubt it can be replied that without a demanding objective nothing will be achieved. Against that, there is the danger that if the objective is too ambitious, unduly drastic methods, involving a high risk of failure, will have to be used; and that if the Government appears to be failing in its objectives it may lose all control of events. It may be that the Chancellor's suggestion that no figures should be mentioned is partly a reflection of these dangers.

8. An alternative line of thought which you may wish to explore at the meeting is that the Government should concentrate its efforts on securing some further reduction in pay settlements, with the amount of the reduction being regarded as secondary. There is a widespread belief among pay bargainers that pay restraint lasts for only two years and that in the third year there is always a rebound. If events early in the 1982-83 round seem to bear out that belief it could have serious consequences. By contrast, a third year of deceleration could have a valuable effect on attitudes.

Methods

9. E(82)53 discusses two areas in which Government action could affect the 1982-83 pay round - getting an appropriate economic message across; and policy towards the public sector, especially the public services. It may, in addition, be worth asking whether there is anything more specific the Government could do in the private sector.

The economic message and getting it across

10. The propositions set out in paragraphs 6 and 8 of E(82)53 are all true. They are also utterly familiar to likely audiences. Is there anything that can and should be done to increase their impact: for example, can a number of suitably convincing examples, whether on a national or an international level, be produced of pay restraint generating extra jobs? Is there more that the Government should be doing to convince union leaders of the need for a higher level of profits?

11. Suggestions of this nature might be looked at by the group of officials suggested in paragraph 9 of E(82)53, which we assume that the Treasury would lead.

The public services

12. As the Chancellor points out the Government has deliberately used public service



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pay to give a lead to the economy in the last two rounds. The method has been to give a signal by publishing the pay factor used in setting cash limits. The 4 per cent pay factor announced on 15 September last year has undoubtedly helped to keep public service settlements (except for the police and firemen) below the average for the economy as a whole and to condition expectations generally. It is however doubtful whether it is realistic to seek below average settlements in the public services for the third year running. It would also be difficult to set a satisfactory pay factor. If the message is to be one of deceleration, the pay factor ought to be less than 4 per cent but that might well be thought unrealistic.

13. The position at present is that public expenditure plans for 1983-84 have already been drawn up on the basis of a published general inflation factor, between *File C* 1982-83 and 1983-84, of 6 per cent. In the Chief Secretary's minute of 26 March 1982 about the conduct of the 1982 Public Expenditure Survey, approved by the Cabinet on *File D* 1st April (CC(82)13th Conclusions, Minute 5), it was stated (paragraph 3 of the Annex) that:

"Ministers should consider in September whether in addition to or instead of any departmental bids a general revision should be made of the plans because of changed prospects for inflation, and whether to choose and publish a separate assumption for pay in 1983-84."

If no separate pay factor is published this year, the existing published general inflation factor of 6 per cent may be taken as the implicit "norm". Alternatively, the conclusion may be drawn that the Government is less concerned than in the previous two rounds with restraining public service pay.

14. There is no need for Ministers to settle this difficult issue now and it would be undesirable to do so until the autumn when up-to-date information about prospects for pay and prices is available. It is nevertheless desirable that the problem should be recognised and Ministers may wish to offer some preliminary thoughts on the strategy, in the light of experience in the 1981-82 pay round and the efforts being made by the public service trade unions to achieve greater coordination.

Mr Heseltine's scheme

15. The trade-off between increased public investment and pay restraint advocated

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by the Secretary of State for the Environment is particularly relevant here since it would largely be directed to the public services (and, to a lesser extent, the public trading sector). The Secretary of State has not set out his ideas in detail; but it is not easy to see how they avoid the objections that have been regarded as decisive when previous versions have been considered.

a. They depend on a clear "norm": if the Government simply asks for pay restraint rather than pay increases not exceeding a stated figure it is impossible to establish the sort of trade-off outlined by the Secretary of State in his minute of 27 May.

b. They imply that there is money available beyond the Government's published expenditure plans and that it is up to the unions to decide whether to spend it on pay or on investment. It is usually an essential part of the resistance to pay claims to argue that there is no more money available.

c. There is no necessary link between pay restraint in a particular service and additional investment in that service. The unions therefore have no good argument of self-interest to use to their members.

The Secretary of State for the Environment might be asked to develop his ideas and indicate how he would meet these objections. It will not be possible for the Committee to reach a considered view on the proposals: the aim will be to determine whether they are sufficiently attractive to be worth working up further.

The private sector

16. Particularly if Ministers were to decide against giving a lead through the public services, the general tone of the pay round, so far as that is a valid concept, would tend to be set by the early settlements, which are largely in the private sector. There are obvious risks involved; but the Committee might wish to consider whether there is any way of influencing employers who settle early in the pay round, either directly or through the CBI.

HANDLING

17. It may be convenient to divide the discussion into two main parts:



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- i. the 1982-83 pay round generally; and
- ii. the particular problems of the public services (this could include discussion of the suggestion by the Secretary of State for the Environment).

On the first part, the Chancellor of the Exchequer and the Secretary of State for Employment are likely to be the main speakers, with contributions from the Secretaries of State for Trade and Industry. The Chancellor of the Duchy of Lancaster and the Lord President of the Council may have particular comments on presentation. Mr Sparrow may wish to comment generally, as indeed may other members of the Committee.

18. In the second part, again, the Chancellor of the Exchequer could be invited to open the discussion. The Home Secretary and the Secretaries of State for Education and Science, the Environment, and Social Services (and possibly the Secretary of State for Defence) may all have departmental points to make. Again, the Secretary of State for Employment and Mr Sparrow may have general comments.

19. At an appropriate point in the discussion, you will wish to ask the Secretary of State for the Environment to develop the suggestion in his minute of 27 May.

CONCLUSIONS

20. You will wish the Committee to reach conclusions on the following:

- i. What should be the Government's objectives for the 1982-83 pay round?
- ii. What are the best methods for achieving that objective?
- iii. Is the Government's message, as suggested by the Chancellor of the Exchequer, broadly right? If so, how best can it be got across?
- iv. Does the Committee wish officials, presumably under Treasury leadership, to draw up a programme for urgent action to put the message across? Is there any guidance which the Committee wishes to give officials?



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- v. Is there any action which needs to be put in hand now in preparation for the next pay round in the public services?
- vi. Is there any action beyond that suggested in E(82)53 which should be taken towards private sector employers?
- vii. Does the Committee wish the ideas advanced by the Secretary of State for the Environment to be developed further?

PLG
P L GREGSON

30 June 1982

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