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C(85) 18

8 July 1985

COPY NO 79

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1985 PUBLIC EXPENDITURE SURVEY

Memorandum by the Chief Secretary, Treasury

With the circulation of the 1985 Public Expenditure Survey Report the first stage of the 1985 Survey is now completed. Once again, the principal characteristic of this stage in the Survey has been the submission of large bids for higher spending by virtually every Department.

2. This paper summarises the position reached and makes proposals for the public expenditure planning totals, running costs and manpower in the three years 1986-87 to 1988-89.

EXPENDITURE BASELINE

3. The starting point is the Survey baseline. For 1986-87 and 1987-88 the baseline equals the figures in the 1985 Public Expenditure White Paper (Cmnd 9428) plus the changes announced in the Budget - additional employment measures and higher Reserves - together with a few minor adjustments.

4. For 1988-89 we agreed to construct the baseline for individual programmes by adding 2½ per cent to the provision for 1987-88 (except in the case of Falklands costs); but consideration of the aggregate planning total figure was left until now.

DEPARTMENTAL EXPENDITURE BIDS

5. Although we agreed that additional bids should be made only in exceptional circumstances Departments have, as I have indicated, put forward substantial bids for extra provision on their programmes. These are summarised in Annex A. In total (net of reduced requirements) they rise from £4½ billion in 1986-87 to £6½ billion in 1988-89. In addition nationalised industries' bids for additional external finance in the Investment and Financing Review - which will be discussed in the Ministerial Steering Committee on Economic Strategy Sub-Committee on Economic Affairs (E(A)) very soon - total £1 billion in 1986-87 and between £1/2 and £3/4 billion in the two later years. And proposals for additional provision for local authority current expenditure in England

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have now been agreed which will require an addition of over £½ billion to the Great Britain provision in 1986-87, and probably of similar sums in the two later years.

#### PROPOSALS FOR EXPENDITURE TOTALS

6. Firm control of public spending is central to our economic strategy, and essential if we are to maintain any prospect of reducing the tax burden. Our discussion at Chequers of public spending priorities was conducted on the basis of this fundamental premise.

7. I recognise that some bids for additional provision will be very difficult to resist. Notwithstanding these pressures I believe it to be essential for the success and credibility of our policies that we should hold the planning totals in 1986-87 and 1987-88 to the baseline levels.

8. For 1988-89 the baseline uplift for individual programmes of 2½ per cent was deliberately set somewhat below the expected rate of inflation to allow a margin for the adjustment of priorities between programmes. I propose we now agree that the aggregate planning total for that year should rise by 3 per cent above the level of the preceding year, in line with the Medium Term Financial Strategy assumption for the rate of inflation in 1988-89. This gives planning totals of:

	<u>£ billion</u>		
	<u>1986-87</u>	<u>1987-88</u>	<u>1988-89</u>
	139.1	143.9	148.2

9. I have carefully considered whether any additional bids we may eventually agree to accept can be financed other than by securing offsetting reductions in spending programmes. There are two main possibilities. First, we could allocate part of the Reserves to programmes. Second, higher proceeds from privatisation ("special sales of assets") are in prospect; these score as a negative item within the planning total.

#### THE RESERVE

10. At Budget time we raised the Reserves for the three forward years, then starting with 1985-86, to £5 billion, £6 billion and £7 billion respectively. Now we are rolling the process forward, with 1986-87 (for which the present Reserve provision is £6 billion) becoming the first year.

11. It is too soon to say with confidence how much of the £5 billion Reserve for 1985-86 will be spent. But it is already clear that we cannot hope for significant underspending; and that we must continue to limit access to cases where it is quite unavoidable.

12. Given what we said at the time of the Budget about the need for adequate Reserves, and in the light of what has happened so far since



then, I do not think we could prudently publish plans for the new forward years with Reserves of less than £5 billion, £6 billion and £7 billion. This means no more than £1 billion in 1986-87 and 1987-88 is now available to allocate from the Reserve to programmes.

#### SPECIAL SALES OF ASSETS

13. Successful completion of the enlarged privatisation programme that we now envisage should mean that the existing planned figures for special sales of assets are exceeded, but we are a long way from knowing precisely by how much. The timing of sales is still to be settled and depends on market conditions and other factors outside our control. But I propose we should assume sales totalling £4½ billion, £3½ billion and £3½ billion over the three years of the Survey.

14. While we have always accepted that receipts from privatisation and asset sales (which are of course desirable for their own sake) count towards achieving the public expenditure control total, it is important to recognise - as the markets and commentators undoubtedly will - that they do not enable us to reduce the tax burden on anything like a pound-for-pound basis. This is partly because of their essentially non-recurring nature and partly because they add to the demands on the financial markets, with obvious implications for interest rates. Thus asset sales in no way diminish the need to maintain the tightest practicable control of public expenditure proper.

15. Moreover, even allowing for some additional room for manoeuvre from higher asset sales as well as from the reallocation from the Reserve, I must warn colleagues that we will face very considerable difficulties in holding public expenditure to the totals I propose. Some of the additional bids will, as I have indicated, be very hard to resist, and the options available to make room for them are limited. This year's Survey will, I am afraid, be another difficult one.

#### RUNNING COSTS AND MANPOWER

16. Improving the efficiency and economy with which Departments conduct themselves must continue to be a vital objective of policy, as the Confederation of British Industry have recently observed. This year for the first time running costs are fully integrated into the Survey. Departments were asked to propose cash targets for their running costs over the three Survey years against the background of our aim that the growth in these costs in aggregate should be held ½ per cent below the assumed level of inflation in each of the three years. On manpower, Departments were asked to examine the scope for further savings and to propose an indicative planning total for 1 April 1989, a year beyond the latest published manpower targets.



17. The provision sought for running costs by Departments compared with the targets proposed, is:

	<u>1986-87</u>	<u>1987-88</u>	<u>1988-89</u>
Provision sought by Departments	+ 6.3%	+ 3.0%	+ 2.5%
Assumed Gross Domestic Product deflator less $\frac{1}{2}$ per cent	+ 4.0%	+ 3.0%	+ 2.5%

18. The details are set out in Annex B. The overall increase of 6.3 per cent in 1986-87 proposed is unacceptably high, and the later year figures will only remain satisfactory if we are able to carry forward first year reductions into the later years.

19. The manpower bids - which, clearly, are an important determinant of the running costs bids - are also set out at Annex B. Those for 1987, 1988 and 1989 are uncomfortably large, given the need for a substantial contingency margin, and the Treasury will be looking for savings wherever possible as part of its scrutiny of Departments' proposed running costs provision.

20. Discussions at official level are already in train to clarify the running costs figures, to seek reductions in provision wherever possible, and to reach agreement on tough but realistic targets for each Department. In the light of the conclusion reached at the Prime Minister's 11 June meeting on long-term unemployment, I have asked Treasury officials to look carefully at any running costs and manpower bids which relate specifically to the control of fraud and to the staffing of services whose cost is wholly recovered by fees, with a view to ensuring that these areas are now given a higher priority within overall totals for running costs. I intend to press Departments during the Survey to find offsetting manpower and running costs savings elsewhere wherever possible.

#### PAY ASSUMPTION

21. In recent years we have considered in the early autumn the public service pay factor or pay assumption for the following financial year. And spending programmes have been reduced ("clawback") by the difference between the figure agreed and the uplift factor originally used to create the Survey provision for that year.

22. I suggest that once again we consider in September this year whether to adopt a pay assumption for 1986-87, taking account of any new or revised factors such as the introduction of running costs targets. But, even if we do then decide to adopt and publish a pay assumption, I am now clear that it could not credibly be less than the cash uplift factor of 3 per cent underlying the 1986-87 baseline. So I propose that we agree now that there will be no "clawback" exercise during this year's Survey.



SURPLUS LAND AND EMPTY HOUSING

23. We have already set in hand action to make a success of our surplus land and empty housing initiative. This depends on Departments drawing up realistic plans to dispose of almost all of their present surplus holdings by the end of 1987-88. I look to colleagues for their full co-operation in agreeing taut targets for disposal in the Survey.

CONCLUSION

24. I invite colleagues to agree:

a. public expenditure planning totals of £139.1 billion, £143.9 billion and £148.2 billion respectively for the three years 1986-87 to 1988-89;

b. Reserves of £5 billion, £6 billion and £7 billion respectively for those three years;

c. that we should adopt the approach to the targets for running costs, manpower, surplus land and empty housing set out in paragraphs 16-23 above;

d. that I should report back to the Cabinet in early autumn when I have completed discussions with colleagues on their individual public expenditure programmes, and on their targets as in c. above.

Treasury Chambers

8 July 1985

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BASELINE AND BIDS ON DEPARTMENTAL PROGRAMMES  
(excluding local authority relevant current, nationalised industries  
and territorial consequences)

	1986-87		1987-88		1988-89	
	Baseline	Add Bids less Red Req	Baseline	Add Bids less Red Req	Baseline	Add Bids less Red Req
MOD						
FCO - ODA	18,558	424.0	18,861	594.0	19,033	905.0
FCO - Other	1,296	64.5	1,317	83.1	1,350	98.3
EC	603	49.3	619	50.1	635	71.8
IBAP	640	60.0	830	170.0	850	100.0
Domestic Agric	1,277	524.2	1,304	535.0	1,337	539.7
Forestry	713	32.0	699	46.1	717	26.3
DTI	53	2.3	54	2.2	56	1.3
ECGD	1,162	57.4	980	56.8	1,004	55.8
Energy	78	163.6	-43	135.9	-44	45.2
Employment	294	-0.5	293	-0.5	300	0.0
Transport	3,704	-19.8	3,901	-24.3	3,999	87.9
DOE - Housing	1,955	134.0	1,995	158.0	2,045	222.0
DOE - PSA	2,424	728.0	2,526	1,013.0	2,589	900.0
DOE - Other	-120	13.5	-128	23.5	-131	33.5
Home Office	848	125.2	860	125.9	882	121.6
LCD	1,061	56.9	1,104	53.8	1,131	69.2
DES	574	60.1	610	80.7	625	117.6
OAL	3,418	96.5	3,505	109.5	3,593	104.0
DHSS - Health(1)	333	17.5	342	27.3	350	37.9
DHSS - Soc Sec	14,945	473.0	15,622	525.8	16,012	958.4
Civil Super	41,547	1,006.4	43,553	1,266.3	44,642	1,711.5
Scotland	1,114	52.0	1,226	74.5	1,257	135.3
Wales	4,300	16.4	4,373	27.4	4,482	0.3
Northern Ireland	1,708	2.8	1,735	2.1	1,779	0.0
Chancellor's Depts	4,464	40.0	4,603	63.5	4,717	93.0
Other Departments	1,825	148.4	1,842	153.0	1,888	114.1
TOTAL BIDS	366	49.9	396	46.1	406	44.5
		4,377.6		5,398.8		6,594.2

(1) includes late bid for NHS pay



## RUNNING COSTS AND MANPOWER BIDS - OVERALL POSITION

## RUNNING COSTS

	1985-86	1986-87	1987-88	1988-89
	£m	£m	£m	£m
Chief Secretary's proposed targets	14,068	14,631 (+4.0%)	15,070	(+3%) 15,446 (+2.5%)
Departments' proposals	14,068	14,958 (+6.3%)	15,414	(+3%) 15,808 (+2.5%)
Differences	-	+327	- +344	- +326

## MANPOWER

	1 April 1986	1 April 1987	1 April 1988	1 April 1989
(1) Cmd 9428 Departments' manpower plans (excluding contingency margin)	598,925	591,939	580,447	-
(2) Contingency margin	6,000	8,500	10,000	-
(3) Departments' proposals (excluding contingency margin)	596,793	595,430	588,554	589,784
Difference (3-1)	-2,132	+3,491	+8,107	
Residual Contingency Margin (if all bids are conceded)	8,132	5,009	1,893	