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10 August 1981

T. Lankester, Esq.,  
Private Secretary,  
10, Downing Street

Dear Tim,

MONTHLY NOTE TO THE PRIME MINISTER ON THE CENTRAL GOVERNMENT,  
BORROWING REQUIREMENT

.... I am enclosing this month's note for the Prime Minister. The main points are summarised on the first page. The borrowing requirement in July was again high - £1,981 million - but £1½ billion of this is attributed to the effects of the Civil Service dispute. In briefing on the money statistics for banking July which were released last Tuesday, we have already revealed that the effect of the strike was large in July, so the outcome for the CGBR in calendar July will not come as a surprise. The note also provides estimates of the "underlying" CGBR to the end of October.

.... With the strike now ended, it will be helpful for the Prime Minister to have an assessment of the speed with which the delayed revenue may be recovered, and the monetary implications of this. The picture is set out in the attached tables.

You will have seen that in briefing on last week's monetary statistics, the Treasury briefed the Press that clearing the backlog would take several months. Our aims were:

(a) to allay fears that there would be acute pressures on the money markets and hence on interest rates caused by surge of revenue.

(b) To prevent expectations developing that the next two months money figures would be exceptionally good.

The following points emerge from the tables:

(i) By the end of July - the formal end of the strike - the loss of revenue, net of VAT repayments held up, was £6-6½ billion. The table does not include the small amount of expenditure also held up, mainly payments to farmers, which might total £250 million. This is expected to be cleared by the end of September.

/(ii) In the



(ii) In the first 2 months there is likely to be little net recovery. By the end of August there is likely to have been no net progress in reducing the net amount outstanding. This reflects a number of factors. First, Inland Revenue think that it may take some time before even normal tax flows are restored and that arrears will for a time continue to mount. The small payers who have not been paying may not respond voluntarily just to the announcement that the strike is over. Restoration of the normal flow in full will require updating of the computer files. Secondly, relatively little of the backlog of tax is in the form of received but uncleared cheques which can be processed rapidly. Thirdly the net flow of VAT revenue in August should be more or less normal, but because Customs and Excise (on Ministerial authority) are giving priority to repayments, the amount of extra VAT repayments is expected to be approximately equal to extra payments coming in. Even in September the net recovery of revenue to the two Revenue Departments together, is expected to be small.

(iii) By the end of the calendar year there could still be £4 billion outstanding and £2 billion by the end of the financial year.

(iv) The permanent costs of the strike are likely to be between £500 million and £1,000 million. About £200 million of the delayed revenue will probably never be recovered (although we will never really know) and the debt interest costs even in 1981-82 will probably exceed £500 million (see Table 2).

(v) The net effect of the strike on the CGBR in 1981-82 could be over £1½ billion. This is made up of the £2 billion still outstanding at the end of the year, less the £900 million or so carried forward from last year, plus over £500 million of additional interest charges. This could mean that the CGBR/PSBR will exceed the Budget estimate though the underlying picture appears to be somewhat better than forecast though not necessarily by enough to cancel out the strike effect.

It may be that Tax Offices will be able to develop ways of speeding up the inflow and the civil sense of taxpayers will be greater than expected. The Chancellor is asking Lord Cockfield to conduct a special study of unconventional ways in which we may be able to speed up the flow of revenue. Nothing may come of it: the experience of the 1979 Post Office telephone billing dispute suggests that recovery of delayed receipts will be long drawn out; and the estimates already assume that staff in tax offices will be fully co-operative after the strike. However that may be, the attempt should certainly be made.



The dispute has of course substantially distorted the monetary statistics. In the first five months of the target period (to mid-July),  $\pounds M3$  increased by 7 per cent, of which about 4 per cent may have been due to the strike. We cannot be precise as we do not know how businesses have allocated the boost to their liquidity between deposits (which would raise  $\pounds M3$ ) and repayment of bank borrowing (which would reduce  $\pounds M3$ ). But our published estimate that the growth of  $\pounds M3$  has been within the target range is based on the reasonable assumption that between 40 and 60 per cent of the deferred revenue has found its way into money. The strike effect on  $\pounds M3$  will fall away as the recovery proceeds. But by the end of the current target period, the level of  $\pounds M3$  may still be 1-2 per cent higher as a result of the strike.

We do not expect the money figures to improve for some time. In banking August, the strike may on balance still be adding to money and in September the effect may be more or less neutral.

One beneficial side effect of the protracted recovery is that it is unlikely that the unwinding will in itself generate acute money market pressures or higher interest rates.

By contrast the strike is likely to delay the start of taxation of unemployment benefit beyond the planned date of April 1982, but it should be possible to start the scheme early in the financial year.

*Yours ever  
Peter*

P.S. JENKINS

TABLE 1

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## CIVIL SERVICE STRIKE AND RECOVERY - EFFECTS ON CENTRAL GOVERNMENT REVENUE

£ million

	1981-82							1982-83		Irrecoverable		
	1980-81		1981 Q1		1981 Q2		1981 Q3		1981 Q4		1982 Q1	Whole year
			July	August	Sept							
Inland Revenue and National Insurance	-610	-3140	-1400	-50	+730	+1950	+1540	+830	150			
Customs and Excise receipts	-470	-1780	-800	+400	+300	+650	+700	+950	50			
Customs and Excise VAT repayment	+200	+1300	+500	-300	-500	-1200	-	-				
NET REVENUE	-880	-3620	-1700	+50	+530	+1400	+2240	+1780	200			
Cumulative net effect on CG revenue	-880	-4500	-6200	-6150	-5620	-4220	-1980	-200				

TABLE 2: INTEREST COST OF THE STRIKE<sup>(1)</sup>

£million

	<u>1981Q1</u>	<u>1981Q2</u>	<u>1981Q3</u>	<u>1981Q4</u>	<u>1982Q1</u>
<u>Approximate cumulative effect of strike on CGBR</u> (including effect on expenditure and debt interest as well as lost revenue)	900	4500	5900	4600	2500
<u>Interest costs</u>					
<u>Within quarter</u>		75	185	160	110
<u>Cumulative</u>		75	260	420	530

(1) Assuming that short-term interest rates stay near their current level for the remainder of the financial year.

MONTHLY NOTE ON THE CENTRAL GOVERNMENT BORROWING REQUIREMENT

Outturn for July and Forecast to end-October 1981

Summary

- the provisional estimate of the CGBR in July is £1,981 million, including the effects of the strike.
  
- about £1 $\frac{3}{4}$  billion reflects delays in tax and national insurance collected. Apart from this, the CGBR would have been about £1 $\frac{1}{2}$  billion, £1 $\frac{1}{2}$  billion better than forecast a month ago, mainly due to timing differences.
  
- the cumulative CGBR to the end of July is estimated at £9,377 million.
  
- for the seven months to end-October the underlying CGBR (excluding strike effects) is forecast to be £6-6 $\frac{1}{2}$  billion, somewhat lower than last year. The actual CGBR will be considerably higher.

CGBR IN JULY

1. The provisional estimate of the CGBR in July is £1,981 million bringing the cumulative total for the financial year to £9,377 million. The figures will be published on Tuesday 11 August.
2. It is estimated that up to £1 $\frac{3}{4}$  billion of tax and national insurance receipts were delayed as a result of the civil service dispute in July. Apart from this the outturn would have been just over £ $\frac{1}{4}$  billion, that is, nearly £ $\frac{1}{2}$  billion better than forecast. As in previous months, lower lending to local authorities and public corporations accounted for much of the difference. The improvement on other items are thought to be largely problems of timing.
3. Table 1, attached, presents a detailed comparison of the forecast and outturn for July. The presentation below identifies the main differences, distinguishing between effects of the strike and other factors. Taken together, the CGBR in July was around £1 $\frac{1}{4}$  billion higher than the forecast excluding the strike included in last month's note.
- Outturn: July: Difference from forecast

	Effect on CGBR (-means adverse)
<u>Strike effects on revenue</u>	
Inland Revenue taxes	)
National Insurance contributions	)
(included in 'other funds and accounts')	)
(          in table 1	)
	-1,350 (approx)
National Insurance Surcharge	)
(Included in Consolidated Fund "other")	)
(          receipts in table 1	)
Customs and Excise taxes	
(net of blocked VAT refunds)	-300
	-----
	-1,650
<u>Other strike effects (net)</u>	
Payments not made (+), some wages not paid (+), additional interest (-)	0 to +30

Other factors

Timing effect of receipts from purchases of certificates of tax deposits (1)	-120
Lower net lending ( to local authorities	+100
( to public corporations	+ 80
Payments across the exchanges to the European Community	+ 70
Payments of Housing Subsidies	+110
Miscellaneous receipts in respect of supply expenditure	+ 60
Other	+160 to +190
	<hr/>
	+460 to +490

(1) the offset of the June purchases mentioned in last month's note.

Strike effects in July

4. As foreshadowed in last month's note the amount of Inland Revenue receipts delayed by the strike during July was, at £1,350 million, rather higher than in June. The Inland Revenue Staff Federation announced its intention of halting receipts of Inland Revenue taxes other than PAYE from the beginning of the month. Nevertheless, the percentage of revenue delayed (27 per cent) was no greater than it had been in April or May.

5. Around £300 million of Customs and Excise net receipts in July were delayed by the strike, about the same amount as in June although rather less in percentage terms.

6. Other financial effects of the strike continued to be small in comparison with the revenue delayed. Selective strikes at MAFF/IBAP continued to delay payments whilst pension payments to former public employees were held up by the escalation of the dispute in the Paymaster General's Office. Partly offsetting these savings, there was a further £60 million or so of interest costs accruing during the month.

Cumulative strike effect to date

7. It is estimated that the cumulative backlog of revenue at the end of July, and hence the end of the strike, was £6-6½ billion. This has been released in the preliminary press notice on the banking-July money supply figures on 4 August.



9. Interest costs on the additional borrowing caused by the strike has risen to an estimated £140 million up to the end of July. This will continue to rise even though the strike is over until such time as the bulk of the revenue delayed has been collected.

#### Other effects in July

9. We continue to be without much of the usual detail because of the dispute.

10. Net Lending to local authorities and public corporations in July was, once again, nearly £200 million below forecast. Local authorities continue to make large repayments to central government, indeed they borrowed very little in total, at least to the end of June.

11. Other effects on central government own-account borrowing in the month were mainly favourable, although thought to be largely timing effects. In particular, last month's forecast included provision for a payment of £70 million across the exchanges by the European Community; in the event only a small payment was made, but the payment in August is now larger than previously allowed for. Also, the expected catching-up in July on a backlog of claims from local authorities in respect of housing subsidies did not materialise.

#### FORECAST FOR THE NEXT THREE MONTHS

12. Even though the strike is now over, the detailed forecasts for August, September and October presented in table 2 do not take account of the expected profile of recovery from the strike and hence will provide a good base against which to monitor the recovery. The effects of the strike will continue to dominate the figures for many months to come. The latest view of the profile of recovery of delayed receipts is discussed in the covering letter.

13. Table 3 shows the outturn/forecast month by month and cumulatively to the end of October both including and excluding strike effects. The underlying 'strike-free' forecast to the end of October would bring the cumulative CGBR to £6-6½ billion, compared with the 1980-81 CGBR of £8 billion in the same period. In particular, the underlying CGBR in October is forecast to be a net repayment compared with small net borrowing in the month last year; the first instalment of the special tax on banking deposits and receipts from the forthcoming sale of Cable and Wireless (each worth just under £200 million) are expected in the month.

14. After allowing for the effects of the strike, the cumulative CGBR to the end of October is expected to be almost £11 billion. Virtually no recovery of the outstanding net revenue delayed by the strike is expected in August; a little more is expected in September and October. By then, the bulk of the money owed by government in VAT refunds should have been cleared and the revenue should begin to come in a little faster.

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TABLE 1

CENTRAL GOVERNMENT BORROWING REQUIREMENT - JULY

	<u>Forecast</u> (excluding strike effects)	<u>Outturn</u> (including strike effects)	<u>Difference</u> <u>on</u> <u>CGBR</u>
<u>RECEIPTS</u>			
<u>Consolidated Fund</u>			
Inland Revenue	3,470	2,499	- 971
Customs and Excise	2,600	2,295	- 305
Other	830	447	- 383
<u>National Loans Fund</u>			
Interest, etc receipts	140	132	- 8
<b>Total Receipts</b>	<b>7,040</b>	<b>5,373</b>	<b>-1,667</b>
<u>EXPENDITURE</u>			
<u>Consolidated Fund</u>			
Supply services and Contingencies Fund	5,800	5,855	- 55
Other	320	314	+ 6
<u>National Loans Fund</u>			
Service of the National Debt	1,440	1,453	- 13
Net Lending	300	181	+ 119
<b>Total Expenditure</b>	<b>7,860</b>	<b>7,803</b>	<b>+ 57</b>
Other funds and accounts	-	+ 449	+ 417
CGBR	- 820	-1,981	-1,161
of which: estimated strike effect	-	-1,650	-1,650
: excluding strike effect	- 820	- 331	+ 489

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TABLE 2

CENTRAL GOVERNMENT BORROWING REQUIREMENT

	Latest Forecast (excluding effect of strike)		
	August	September	October
<u>RECEIPTS</u>			
<u>Consolidated Fund</u>			
Inland Revenue	2,350	4,460	3,470
Customs and Excise	1,880	1,850	2,590
Other	820	750	810
<u>National Loans Fund</u>			
Interest etc, receipts	290	800	410
Total receipts	5,340	7,860	7,280
<u>EXPENDITURE</u>			
<u>Consolidated Fund</u>			
Supply services	5,800	6,100	6,100
Other	420	310	280
<u>National Loans Fund</u>			
Service of the national debt	780	1,220	370
Net Lending	330	800	550
Total expenditure	7,330	8,430	7,300
Other funds and account	+70	+210	+170
CGBR excluding strike effect	-1,920	-360	+150

TABLE 3

## CENTRAL GOVERNMENT BORROWING REQUIREMENT

	1980-81		1981-82		
	In Month	Cumulative	Outturn/Forecast excluding estimated strike effect		Outturn including strike effect
			In Month	Cumulative	
April	0.9	0.9	1.0-1.2	1.0-1.2	2.4
May	2.4	3.3	1.6-1.7	2.6-2.9	2.7
June	1.3	4.6	1.0-1.1	3.6-4.0	2.3
July	0.8	5.4	0.3-0.4	3.9-4.4	2.0
August	1.6	7.0	(1.9)	(5.8-6.3)	(1.9)
September	0.8	7.9	(0.4)	(6.2-6.7)	(-0.1)
October	0.2	8.0	(+0.2)	(6.0-6.5)	(-0.5)
November	2.8	10.9			
December	2.2	13.1			
January	-1.8	11.3			
February	0.7	12.0			
March	0.9	12.9			

Notes: - Forecast for 1981-82 in Financial Statement and Budget Report is £11,497 million.

- Some rows may not add across because of rounding.