

From: The Rt. Hon. Francis Pym, M.C. M.P.

NBPM AT 30/7  
House of Commons,  
London, SW1A 0AA



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They plan  
to purchase his  
circumstances

23rd July, 1985.

24/7

23 JUL 1985	
MR ODLING-SMITH	
CST FST EST MST	
SIR P MIDDLETON	
SIR T BURNS	
MR G WHITE	

Dear Nigel,

RL  
24/7

MR WICKS MR LOVE  
MR CRUPPER  
MR H DAVIES

Thank you for your letter of the 15th July.

We are glad to note how broadly you are in agreement with us about priorities and objectives. In particular, we welcome your assurance that you do not regard unemployment as a necessary consequence of the battle against inflation and that you agree that unemployment is our major social problem.

We share your view of the need for wage restraint since a reduction in the level of real wages relative to the cost of capital will eventually translate itself into more jobs. This is, indeed, one of the reasons why we attach so much importance to sustained capital investment programmes, (and not just a once-for-all upturn due to a change in capital allowances in a particular financial year). However, a reduction in real wages, even if attainable, takes a long time to work its way through the economy and more urgent action is needed if unemployment levels are to start falling soon.

The figure we quoted in our last letter for the average level of assumed earnings of those re-entering the work-force was necessarily illustrative (because no one can be sure what it would be and the Treasury has tended to underestimate future wage rises in the past) but we do not feel that this weakens the general thrust of our argument about the large revenue losses arising from high unemployment. We are glad to note your assurance that the Treasury takes this argument into consideration in determining its advice to you and we hope that you will give greater weight to it in your future public statements.

We would counsel you not to underestimate the second-round effects of public investment. The dramatic fall in the numbers of unemployed in the U.S.A. in recent years, which appeared to surprise some of your advisers in the Treasury, showed how great and progressive an impact these effects can have. American experience also disproves your contention that a reduction in unemployment cannot be the result of additional public expenditure or increased borrowing.

....



We are frankly puzzled by your strictures about "easing up on monetary conditions" at a time when Sterling M3 seems to be almost out of control and bank credit has expanded so rapidly. We favour a tight monetary policy combined with a more flexible fiscal policy.

It is not an expansion of the Money Supply but of the PSBR which is needed. Some among us have long maintained that there is no direct relationship between the PSBR and interest rates. Your own policies have demonstrated this fact anew. After all, the UK has one of the lowest PSBR's in the industrialised world but our interest rates are almost double those of our competitors.

We believe that increased levels of public investment are vital. They can be achieved without irresponsibility over the PSBR. Every pound received from privatisation can, and in our view should, be used to back a concerted strategy for employment, without adverse effect on the PSBR. Such a strategy would include capital investment in such areas as housing, roads and infrastructure generally.

We believe that this would have a beneficial effect on the levels of employment and provide the starting point for that virtuous economic circle to which we referred in our previous letter and which can alone ensure both falling unemployment and the prospect of a continuing regime of tax reductions in the future.

It is our intention to publish this exchange of correspondence.

I am copying this letter to the Chief Whip.

*Handwritten signatures*

*Handwritten signature*  
Alan Haselhurst

The Rt. Hon. Nigel Lawson, M.P.,  
Chancellor of the Exchequer,  
The Treasury,  
Whitehall,  
London,  
S.W.1.