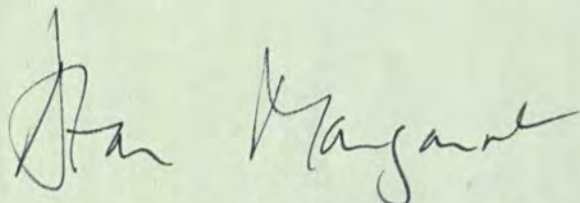


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22 July 1986

The Rt Hon Margaret Thatcher MP
House of Commons
London
SW1A 0AA

B/R 1/10/86.
for speeches.



As the House prepares to rise for the long Summer Recess, I thought it might be useful if, as last year, I took this opportunity to set out how I see the current economic situation and prospects.

I wrote a year ago of the excellent progress the economy has made since we were re-elected in June 1983. That progress has continued. Since I last wrote, output, exports, investment and living standards have all reached new all-time highs; and our growth rate last year, at $3\frac{1}{2}$ per cent, was the highest in the European Community and higher than the United States, too.

And inflation, now down to $2\frac{1}{2}$ per cent, is at its lowest level for almost 20 years. When you compare it with the average rate of inflation of $15\frac{1}{2}$ per cent during the lifetime of the last Labour Government, that is a remarkable achievement by any standards.

The outstanding event on the economic scene during the past 12 months has been the dramatic collapse of the world oil price to little more than a third of its former level - around \$10 a barrel compared with \$27 a barrel a year ago.

This affects us in a number of ways, some bad, some good. It clearly implies some deterioration in the current account of the balance of payments, and the massive fall in our North Sea oil revenues inevitably limits the scope for reducing the burden of non-oil taxation, at least in the short-term.

But perhaps the most important consequences are the indirect ones, via the effects on world activity and world trade.

The initial consequences have been unfavourable, as those nations and regions that are heavily dependent on their earnings from oil have had to tighten their belts as rapidly as they can. By contrast, the great benefit to oil consumers (which means above all the industrialised world) has so far been felt in terms of higher real income and profitability: the increased activity that this should generate has yet to appear.

I believe it will, and before this year is out. Meanwhile, the way in which we have successfully weathered the unprecedented collapse

in the oil price has exploded once and for all the myth that our new-found economic strength was wholly dependent on North Sea oil. While there has been some inevitable adjustment in the exchange rate, it has occurred in an orderly way. And interest rates are now 2 per cent lower than they were a year ago, while our foreign exchange reserves have actually risen by over 30 per cent.

But the pause in world economic growth not only means that I now expect growth this year to be a little below the 3 per cent I forecast at the time of the Budget. It is also one reason why, despite all the measures we have taken to combat the scourge of unemployment, the numbers out of work have gone on rising and seem likely to rise further in the immediate future, at least until the pause is over.

And this is despite the fact that there are now very nearly a million more jobs in this country since the last General Election - a bigger increase than the whole of the rest of the Common Market put together.

A major cause of high unemployment is that labour costs in Britain continue to rise much too fast - and, in particular, faster than among our major competitors overseas. With inflation down to 2½ per cent, and the overall cost of living, thanks to the tax cut in the Budget, only ½ per cent higher than a year ago, it is madness for companies to increase wages at the rate they are. The result can only be higher unemployment.

The responsibility for getting a firm grip of their wage costs lies fairly and squarely with management. But I have sought to help by campaigning for the wider adoption of profit-related pay. The advantage is twofold: the greater sense of identification between employees and their companies if part of their pay is explicitly linked to profitability, and the greater degree of pay flexibility that results. And I have indicated my readiness to consider a measure of tax relief for such schemes. This is all set out in my recent Green Paper on profit-related pay.

I originally announced this in the Budget, at the same time as I published a Green Paper on the reform of personal taxation, setting out a scheme to remove the discrimination in our tax system against married women. I have also recently published further details of another initiative I launched in the Budget: the Personal Equity Plan. This pioneering scheme, which will come into force on January 1st, will enable small investors to invest directly in the shares of British businesses without having to pay a penny piece in tax.

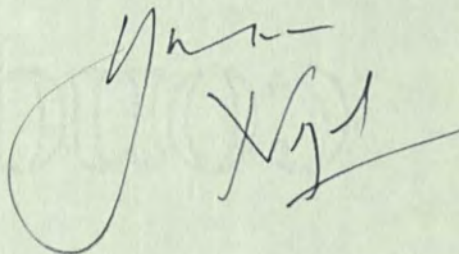
Recent surveys suggest that, since we first took Office, the proportion of adults in this country directly owning stocks and shares has doubled. With the continuing privatisation programme - including British Gas this autumn - as well as the Personal Equity Plan scheme, the prospects for still wider share ownership are excellent. Nor shall we allow Labour's crude threats of renationalisation on confiscatory terms to stop us.

This year's Budget demonstrated two further things: first our continuing commitment to reducing the burden of income tax, and second, the caring nature of Conservatism, with the most far-reaching package of assistance to charitable giving ever - as the charities themselves were the first to acknowledge. I am enclosing a separate note about this last, which I hope you will find helpful.

So what of the prospects for 1987? I expect it to be a better year than 1986. The pause in world growth should come to an end later this year, and inflation should stay low. So the prospect for jobs will improve - particularly if pay settlements respond to the sharp fall in inflation, as they already have in our major overseas competitors.

Meanwhile, the fact that over the past three years we have successfully survived both a 12-month long coal strike and an unprecedented collapse in the price of oil is the clearest possible demonstration of a strong economy and sound policies. It is this, above all, that enables us to face the future with confidence.

NIGEL LAWSON

A handwritten signature in dark ink, appearing to be 'Nigel Lawson', written in a cursive style. The signature is positioned to the right of the typed name 'NIGEL LAWSON'.

THE CHARITIES INITIATIVE

I am sending to all Members copies of two new Inland Revenue pamphlets about tax relief for charitable giving. Among other things they describe the new payroll giving scheme, and the new tax relief available to companies wishing to make annual donations without having to covenant.

I believe these schemes will come to be seen as one of the most significant of this Government's innovations. It is vitally important that they become well established in the public consciousness before the General Election. They therefore need all the publicity they can get in the next few months.

The impetus for a broad take-up of the new tax reliefs must come mainly from the charities themselves. They must encourage companies to step up their donations to the limits allowed under the legislation; they must encourage employers and employees to agree among themselves to setting up payroll giving schemes.

Members of Parliament can play a major role in galvanising other people into action. May I ask you, during the coming months, to go out and:

- * Press charities in your constituency to take advantage of the new opportunities. This is the most important: they must 'sell' the new reliefs to potential donors.
- * Inform local companies of the new and more advantageous way they can give to charity.
- * Tell local employers of the simple way in which they can set up payroll giving schemes for their workforce.

The company donation scheme is operative as from now. The payroll scheme comes in for the tax year starting next April, but preparatory work will need to be done well in advance.

N.L.

CONQUIEROR

