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PRIME MINISTER

BUDGET ARITHMETIC

A brief note on the Budget arithmetic may be useful before today's meeting on social security matters.

2. As you know, I envisage that in the Budget:-

- (a) Most specific duties would be fully revalorised.
- (b) For industry there should be a further $\frac{1}{2}$ per cent NIS cut from August, some concessions (which I am still discussing with Nigel Lawson) on the North Sea oil regime, and some movement on Corporation Tax.
- (c) For individuals I envisage a major increase in the thresholds - perhaps $8\frac{1}{2}$ percentage points, over Rooker-Wise (5.4 per cent), for all bands and rates. I also hope to increase child benefit substantially - hopefully taking it back to its level in April 1979
- (d) I am also putting together a series of lesser measures to assist enterprise and small firms, technology and innovation, construction, and charities - including a major (but not in-expensive) simplification of the Business Start-Up Scheme.

3. The PSBR cost of the Budget measures in 1983-84 is of the order of £1.6 billion to £1.9 billion. The comparable costs for 1984-85 are about £1.9 billion to £2.4 billion.

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4. These figures have to be seen against our present estimate - which may contract - of "fiscal adjustments" - that is, room for manoeuvre - of £2 billion for 1983-84 and between £2.5 and £3 billion for 1984-85. If this week's forecast narrows the room for manoeuvre (and it looks likely to do so), I would be driven to the lower figures in paragraph 3 above, and might if necessary have to pare down some of the measures described in paragraph 2 above - not least because we must be able to show a reasonable "fiscal adjustment" remaining for 1984-85. But I would hope that the main measures would stand, for they constitute an effective package, split almost exactly equally between businesses and persons (taking into account measures announced in the Autumn), and would be seen as politically helpful while also continuing our prudent monetary and fiscal policies. (There would be a continued reduction in planned borrowing.)

5. But overhanging all this is the question of the social security over-provision. The amount at stake here amounts to some £180 million in 1983-84 and £530 million in 1984-85. If we were to have to drop all action to deal with the over-provision, and also to proceed with some of the attractive concessions which we have been considering, with Norman Fowler, the figures would rise to £250 million in 1983-84 and £725 million in 1984-85.

6. You will see that these amounts would have a very serious effect on the Budget arithmetic. If the fiscal adjustment does have to be revised downwards in response to the latest forecasts, some of the key paragraph 2 measures would have to be dropped. Even if no revision proves necessary, following the forecast, we would still be left with a derisory, or negative, fiscal adjustment for 1984-85. Moreover, the public expenditure position, particularly for 1984-85, would be particularly difficult.

7. In short:-

- (a) If the forecast turns against us we shall have to keep the cost of our Budget measures to the lower figures in paragraph 3 (or even lower), which means omitting some attractive measures.



(b) If in addition we were to drop action on social security over-provision, the result would be a most unattractive Budget: a relatively small amount of reliefs etc, with (certainly in the second year) the social security beneficiaries taking a very large part, leaving relatively little for the rest of the personal sector and for industry.

8. It follows that, whether we proceed by the Chief Secretary's route or by Norman Fowler's, we really must act on the over-provision. My preference is for the Chief Secretary's route, because I judge it easier to win that way in the House. But win we must: that is the key point.

Margaret O'Hara

for (G.H.)

21 February 1983

*(approved by the Chancellor and signed
in his absence)*