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PRIME MINISTER

BILATERAL WITH THE CHANCELLOR

The Chancellor will want to devote the meeting almost entirely to public expenditure. He will begin with a discussion of developments since Chequers and is likely to express his concern about the views of the Lord Privy Seal as they have emerged from his speech and his lobby briefing. The Chief Secretary is scheduled to join the meeting at 17.45. The main business will be to clear the papers for next week's public expenditure Cabinet and the E(A) meeting on nationalised industries. Drafts of the papers are attached:-

- Economic prospects Flag A
- 1985 Public Expenditure Survey Flag B
- Nationalised industries: 1985 investment and financing review Flag C

The main issues are:-

- i) What should be set aside as the Contingency Reserve? Experience confirms the wisdom of substantial reserves and the Chief Secretary recommends £5b., £6b. and £7b. This would allow only £1b. of the Reserve in each year to be allocated to programmes as the Reserve is rolled forward.

- ii) What should be assumed for asset sales? The White Paper assumes sales of £2¼b. in 1986-87 and 1987-88. Clearly the figures will be higher than this with the sale of BGC. The Treasury suggest raising the figures to £4½b., £3½b. and £3½b. over the three years of the survey. The aim should be to set the lowest figures that is credible to the colleagues in order to leave room for a small upward

adjustment at the end of the round if that proves necessary.

iii) What should the planning total be?

In order to give the Chief Secretary and the Star Chamber an objective that can be realised the figure should be tough but realistic. The Treasury suggest setting the planning totals at the same level as in the Budget. The increase in asset sales effectively allows an extra £2½b., £1½b. and £1½b. to be added to programmes. (This in addition to the £2b. a year increase made in the planning total in the Budget).

iv) How should negotiations on manpower be conducted?

There is an outstanding remit to consider more sympathetically increases in manpower which improve revenue e.g. from expanding services financed by fees, improving tax in-flows or cutting down on benefit fraud. The Chief Secretary wants to avoid making this remit a separate exercise as he fears that in doing so the Treasury would be knocked down in the rush as it was with 1982 local authority capital expenditure. The Chief Secretary prefers to deal with this issue in the normal way, though with revenue increases as a factor to be taken into account.

v) Should the E(A) meeting precede or follow the Cabinet meeting?

Normally the E(A) discussion has preceded Cabinet but this year the Treasury suggest holding it after. The reason for this is because the targets being set for nationalised industries appear modest e.g. getting back to base line in 1986-87. In practice these are tough targets because the privatisation of BGC removes the contribution which gas has been making and the electricity industry is seeking increases as

a result of the need to increase coal stocks.
Circulating such apparently easy targets before
Cabinet might give the wrong signals.

A. S. L.

pr.

Andrew Turnbull

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