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CABINET

CONCLUSIONS of a Meeting of the Cabinet  
held at 10 Downing Street on

THURSDAY 16 FEBRUARY 1989

at 10.30 am

P R E S E N T

The Rt Hon Margaret Thatcher MP  
Prime Minister

The Rt Hon Sir Geoffrey Howe QC MP  
Secretary of State for Foreign and  
Commonwealth Affairs

The Rt Hon Nigel Lawson MP  
Chancellor of the Exchequer

The Rt Hon Lord Mackay of Clashfern  
Lord Chancellor

The Rt Hon Douglas Hurd MP  
Secretary of State for the Home Department

The Rt Hon Peter Walker MP  
Secretary of State for Wales

The Rt Hon George Younger MP  
Secretary of State for Defence

The Rt Hon Norman Fowler MP  
Secretary of State for Employment

The Rt Hon Tom King MP  
Secretary of State for Northern Ireland

The Rt Hon Nicholas Ridley MP  
Secretary of State for the Environment

The Rt Hon Lord Young of Graffham  
Secretary of State for Trade and Industry

The Rt Hon Kenneth Baker MP  
Secretary of State for Education  
and Science

The Rt Hon Kenneth Clarke QC MP  
Secretary of State for Health

The Rt Hon John MacGregor MP  
Minister of Agriculture, Fisheries  
and Food

The Rt Hon Malcolm Rifkind QC MP  
Secretary of State for Scotland

The Rt Hon John Moore MP  
Secretary of State for Social Security

The Rt Hon John Wakeham MP  
Lord President of the Council

The Rt Hon The Lord Belstead  
Lord Privy Seal

The Rt Hon Cecil Parkinson MP  
Secretary of State for Energy

The Rt Hon John Major MP  
Chief Secretary, Treasury

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THE FOLLOWING WERE ALSO PRESENT

The Rt Hon David Waddington QC MP  
Parliamentary Secretary, Treasury

The Rt Hon Peter Brooke MP  
Paymaster General

SECRETARIAT

Sir Robin Butler  
Mr R T J Wilson (Item 5)  
Mr R G Lavelle (Items 3 and 4)  
Mr P J Weston (Items 3 and 4)  
Mr A J Langdon (Items 1 and 2)  
Mr G Monger (Item 5)  
Mr S S Mundy (Items 1 and 2)

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PARLIAMENTARY  
AFFAIRS

Food Safety

Previous  
Reference:  
CC(89) 5.2

1. The Cabinet were informed of the business to be taken in the House of Commons in the following week.

THE SECRETARY OF STATE FOR HEALTH said that on the following day The Lancet would carry a Public Health Laboratory Service report on listeria which found listeria to be present in fairly large samples of various foodstuffs available to the public. Some indication of the contents of this report had become known the previous week, and that had led the Chief Medical Officer to issue guidance to the public on Friday 10 February. That guidance had warned pregnant women and certain other groups that were at high risk from listeriosis not to eat certain foods such as soft cheese, and to take specified precautions on the preparation of other foodstuffs such as pre-cooked poultry and pre-cooked chilled meals. The Opposition had chosen food and water safety as the subject for debate on the following Tuesday, but he believed that the range of action being taken by the Government was producing a more settled atmosphere and that the Opposition would rightly be perceived as irresponsibly trying to stir up public hysteria. One point on which he was acting was to stipulate the temperature at which pre-cooked chilled foods should be stored in all food businesses: he had now received the necessary advice from the experts that 5°C was the appropriate temperature for this purpose and he had made it known that he would prescribe this under the Food Hygiene Regulations as soon as possible. Mr Robin Cook, the Opposition spokesman on health, had confused this issue with the entirely separate question of the cook-chill catering system as used in the National Health Service. The relevant Department of Health guidelines for this system, which had been issued in 1980, prescribed 4°C as the appropriate storage temperature and Mr Cook was suggesting that this figure, rather than 5°C, was the one that should be specified for pre-cooked chilled foods under the Food Hygiene Regulations. He would need to deal with Mr Cook's confusion in a way that denied Mr Cook the opportunity to claim that he had put forward the lower figure with the public's interests at heart.

THE PRIME MINISTER, summing up a brief discussion, said that action was in hand on the specific food safety issues that had been identified in recent weeks, but that public awareness had been raised on matters of food safety and of hygiene generally, and new areas of concern might emerge with little notice. One such public health matter that was coming to attention was the increase in numbers of rats following two mild winters in succession. It was a matter of common observation that restaurants and other businesses were in the habit of leaving inadequately packaged perishable refuse on the pavement. This was unacceptable, and the increase in rats made a bad situation worse. The time might be coming when legislation would have to be introduced to place a duty on businesses to dispose of their refuse in a proper fashion.

The Cabinet -

Took note.

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HOME AFFAIRS  
Unemployment  
Previous  
Reference:  
CC(89) 2.2

2. THE SECRETARY OF STATE FOR EMPLOYMENT said that the unemployment figures for January would be published that day. The seasonally adjusted total had fallen by 49,300 to 1.988 million. The reduction in unemployment below two million, for the first time for around eight years, would be seen as a very important milestone. This was the 30th consecutive monthly reduction, and the rate of unemployment had fallen to 7 per cent, which was below the European Community average and, in particular, was below the rates in Italy, France, Belgium, the Netherlands, Spain and the Republic of Ireland as well as Canada. The Opposition would seek to distract attention from these very welcome reductions in unemployment by contending that the figures had been artificially depressed by means of various changes in the definition of unemployment. The Opposition were claiming that the real level of unemployment stood at something over three million, but the forthcoming Labour Force Survey for 1988 was expected to confirm the trends shown by the monthly unemployment statistics. The Labour Party manifesto at the previous General Election had claimed that a Labour Government would reduce unemployment by 1 million within two years, but this now contrasted unfavourably with the actual reduction of 966,000 which had been achieved in the period since the General Election campaign. The unadjusted total of unemployment had increased by 28,000 to 2.074 million in the period since December 1988. This total invariably rose in the period after Christmas, and the increase on this occasion had been relatively slight compared with previous years. While it was true that, as a result of the relatively mild winter, there had probably been fewer unemployed than in previous years among workers in the construction industry, the favourable weather conditions would have done little to stem the significant number of redundancies which regularly occurred in certain industries, notably tourism, in the period immediately following Christmas. An especially encouraging feature was that, at a time when seasonally adjusted unemployment had fallen consistently by around 40-50,000 over each of the previous few months, the estimated number of vacancies in the economy as a whole had remained at about 700,000 throughout that period. He would also be issuing figures later that day which showed that there were now 145,000 people in training under the Employment Training programme. This was a remarkable achievement over a period of less than five months since the programme was launched, and the success of the programme demonstrated that, even though the trend of unemployment had been very favourable in recent months, the Government was far from complacent. The number of people in work had never been higher, even excluding those in training.

THE PRIME MINISTER, summing up the discussion, said that the position on unemployment and employment remained very encouraging.

British  
Aerospace PLC

THE SECRETARY OF STATE FOR EMPLOYMENT said that British Aerospace PLC would be announcing that morning two and a half thousand redundancies in its dynamics division. This was part of a relocation and rationalisation package, which had been planned for some time, in which the number of sites would be reduced from six to four with the closure

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of the plants at Bracknell and Hatfield, which were areas of relatively low unemployment where the company had been experiencing recruitment and retention difficulties. Some of the jobs would be switched to Bolton and Plymouth, and this would create welcome employment opportunities in areas where the rate of unemployment was higher than average.

The Cabinet -

took note.

FOREIGN AFFAIRS

Anglo-Iranian relations

Previous reference: C(88) 34.3

3. THE FOREIGN AND COMMONWEALTH SECRETARY said that the reaction from Ayatollah Khomeini of Iran to Mr Salman Rushdie's book "The Satanic Verses" called to mind the fanaticism of other religions in the past, including those within the Western tradition. What made matters more difficult to handle now was the propagation worldwide of local reactions through the media, especially television, as well as the fact that there were many representatives of such creeds as Islam spread widely through the international community. A further complication was the continued detention in Iran of Mr Roger Cooper, and uncertainty over the recent statement that a "heavy" sentence had been passed on him. It was necessary for the Government to make clear that the public threat against Mr Rushdie's life was unacceptable and that such behaviour by Iran was incompatible with the maintenance of proper relations between the two countries. But the Government should avoid complete rupture with Iran. The British Charge d'Affaires had called on the Iranian Ministry of Foreign Affairs to enquire about the sentence on Mr Cooper, to express strong disapproval of Ayatollah Khomeini's action and to obtain assurances on the protection of the British Embassy premises in Tehran which had been the subject of a demonstration on 15 February. The Ministry of Foreign Affairs had taken the line that they could not erase what had been said by the Ayatollah but they would continue to protect the British Embassy. It appeared that they wished to do what they could to mitigate the effects of extreme reactions in Iran to Mr Rushdie's book. The Iranian Foreign Minister, Dr Ali Akbar Velayati, whom he had seen the preceding week, had also been trying in public statements to put matters in a more balanced context.

The Iranian Foreign Ministry had said that consular access to Mr Cooper would be granted within the next two weeks and that visas for his family to visit him in Iran would also be made available. Mr Cooper's brother, realising that anything he said could affect the fate of Mr Cooper, was behaving with dignity and restraint. The risk that the crusade against Mr Rushdie's book would be taken up by the Islamic Conference as a whole seemed to be containable. It appeared for example from reaction to the demonstration in Pakistan against the United States Embassy in this connection that the Pakistan Government were anxious to maintain a balanced position, despite the fact that five people had been killed and 200 injured by the Pakistan security authorities in their attempts to control the demonstration. His Department intended to call in the Iranian Charge d'Affaires in London to express to him the Government's disapproval of Ayatollah Khomeini's threat which amounted to direct

interference in United Kingdom internal affairs. His Department would make it clear that there could be no further extension of the British presence in Tehran nor increase in the Iranian presence in London in the circumstances. It was nevertheless important to try to maintain a thread of contact with the saner elements in the Iranian regime. The British press had shown a helpful awareness that the Government had a difficult balance to strike.

THE HOME SECRETARY said that incitement to murder was a serious offence. The police on their own responsibility had taken the sensible decision to provide some protection for Mr Rushdie. They were also investigating comments alleged to have been made by the Bradford Muslim leader, Sayed Abdul Qudus, to see whether he had committed an offence. The possibility of public disorder could not be excluded. He was in touch with the Chief Constables in the cities principally concerned as well as with Conservative Members of Parliament with constituencies in such areas. He had also been over the ground with President Ershad of Bangladesh who was currently visiting the United Kingdom and who had shown understanding of the Government's position. It would be important to measure words carefully in any public statements on the subject.

THE PRIME MINISTER, summing up a brief discussion, said that the basic point was that the law of the United Kingdom had to be upheld. It would be necessary to look very carefully at the credentials of applicants seeking to visit the United Kingdom from Iran, in the light of the threat against Mr Rushdie's life.

Jamaica

THE FOREIGN AND COMMONWEALTH SECRETARY said that the result of the election in Jamaica on 9 February had been a victory for Mr Michael Manley of the People's National Party by 45 seats to 15, with 57 per cent of the vote. This result unfortunately continued the tradition in Jamaica whereby no leader had been able to gain a third term. However, the level of violence associated with the election had been lower than feared. Mr Manley's initial statements suggested a policy stance less unhelpful now than that implied by his record in office during the 1970s.

Sri Lanka

THE FOREIGN AND COMMONWEALTH SECRETARY said that the results of the current elections in Sri Lanka had not yet come through. The expectation was that President Premadasa's party would be returned. There had been some 400 deaths associated with the electoral campaign.

Previous Reference: CC(88) 40.2

European Community Foreign Ministers' Meeting in Madrid

THE FOREIGN AND COMMONWEALTH SECRETARY said that he had attended a good session of European Community Foreign Ministers in Madrid on 14 February, meeting in the framework of European political co-operation. There had been a helpful discussion on the Middle East against the background of the Presidency mission by the Spanish Foreign Minister, Senor Fernandez Ordonez, which had been sensibly carried out.

There was general agreement on the need for European influence on and support for the key role of the United States in the Arab/Israel dispute. The Ministers had also welcomed and compared notes on the tour of Europe by the new United States Secretary of State, Mr James Baker. The expectation was that there would be a Summit in May of the Heads of State or Government of the North Atlantic Treaty Organisation. There had been condemnation of the human rights situation in Romania. The Twelve Ministers had released a statement on Afghanistan urging all parties to try to establish a united and fully representative government. Following the withdrawal of Soviet troops, it was noteworthy that Poland and Hungary had closed their Embassies in Kabul, which was a conspicuous expression of their lack of confidence in Mr Najibullah's regime. The Twelve Ministers had also issued a statement welcoming the opening of round table talks in Poland involving representatives of the Polish Government and the different political and social forces in that country. On South Africa there was further recognition by other European Foreign Ministers that economic pressure was not the best way forward, particularly given the changes which had come about in relation to Namibia and Angola. The Twelve had issued a statement on the Code of Conduct for Community companies with subsidiaries in South Africa, noting the role that these companies played in promoting the interests of their black employees and in encouraging businesses run by black people.

The Cabinet -

Took note.

COMMUNITY  
AFFAIRS

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Agriculture  
Council,  
13-14 February

4. THE MINISTER OF AGRICULTURE, FISHERIES AND FOOD said that at its meeting on 13-14 February the Agriculture Council had given initial consideration to the Commission's proposals for agricultural support prices for 1989-90. The general approach taken by the Commission was in line with the reform of the Common Agricultural Policy for which the United Kingdom had been working. There were fewer than usual specifically United Kingdom issues raised by the Commission's proposals and also some hope that negotiations might be completed more expeditiously than in the past. If the Commission's proposals were sustained the cost would be below the guideline limit. There was a danger that a number of member countries might seek to use up the existing margin. His principal objective in the detailed negotiations would be to seek to limit erosion of the Commission's proposals.

Continuing, THE MINISTER OF AGRICULTURE, FISHERIES AND FOOD said that he had made a statement at the Council on the problem of fraud. This followed up statements he had made at a number of meetings in the past which appeared to be bearing fruit. The Commission were now committed to action. There had been a good response from the Spanish Presidency to his most recent statement and they had undertaken to put this issue on the agenda for future meetings. In a brief discussion it was noted

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that the problem of traffic across the Irish border had decreased with the reduction in the extent of monetary compensatory amounts (MCAs), and that the intended elimination of MCAs might largely resolve the problem.

Economic and  
Finance  
Council,  
13 February

THE CHANCELLOR OF THE EXCHEQUER said that there had been a meeting of the Economic and Finance Council on 13 February which had been attended by the Economic Secretary to the Treasury. The main item was a presentation by Madame Scrivener of the Commission's proposals for a withholding tax on savings. The tax proposed differed from the composite rate arrangements in the United Kingdom. There might indeed be some awkwardness if revised proposals were to be modelled on the UK system but there appeared to be no likelihood of this. Although the United Kingdom had been in a minority in opposing the Commission's proposals this opposition had been given staunch support by Luxembourg. The Netherlands Finance Minister had also opposed the Commission proposals. It was to be hoped that this position would be maintained. Greece and Ireland had not yet decided what view to take. The French had taken the lead in supporting the proposals. They had sought unsuccessfully at an earlier stage to make agreement to such a tax a precondition for agreement to the capital liberalisation directive. On this point the German Finance Minister had expressed the view at the Council that while no legal link existed there was a political commitment to a tax. The main concern of the French authorities was that when the final stage of implementation of capital liberalisation took place there would be a flight of capital from France and a substantial increase in tax evasion. It had not been the United Kingdom experience that the abolition of exchange controls had led to any increase in tax evasion. What seemed however clear was that a withholding tax would deter investors from placing capital in the Community. This would damage not only individual financial centres but the Community as a whole. The Spanish Presidency had indicated that they would give this proposal a high priority during their period of office with the implication that less priority would be given to carrying forward the Commission's proposals on indirect tax. It had been suggested that if the matter could not be settled beforehand it would need to be brought to the European Council in Madrid for decision.

The Cabinet -

Took note.

PAY REVIEW  
BODY REPORTS

5. The Cabinet considered a note by the Secretary of the Cabinet (C(89)4) about the recommendations of the Pay Review Bodies.

THE PRIME MINISTER said that the paper was the outcome of a discussion among Ministers most directly concerned with the Review Body reports. It proposed that the reports of the Review Bodies on the Armed Forces, on Professions Allied to Medicine, and on Nurses should be accepted in full. The report of the Review Body on Doctors and Dentists should be

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accepted except for the increases at the top of the consultants' scale, and in the size of their distinction awards. These would have given big increases in salary (up to 13 per cent) for consultants. The Review Body said it was proposing them to improve the long-term career structure for hospital doctors. That objective would be better achieved by the increase of 100 in consultants posts proposed by the White Paper, 'Working for Patients', which had been announced after the Review Body's Report was completed. Consultants would still get the 8 per cent across the board increase recommended for all doctors and dentists. The report of the Top Salaries Review Body (TSRB) should also be accepted, subject to a point on two star officers. The Review Body had proposed that they get a proper differential above one star officers, their pay should be linked to the first performance point for Grade 3 civil servants. Linking standard pay to a performance point in this way was however unacceptable. Instead, it was proposed that the pay of two star officers should be around 85 per cent of the normally attainable maximum for Grade 2 civil servants. This would give them the figure recommended by the TSRB, while preserving the necessary link with the Civil Service.

Continuing, THE PRIME MINISTER said that, as to financing, the cost of the awards for the armed forces and the TSRB groups could be met from current provision. For the National Health Service (NHS) groups, the cost in excess of current provision was £248 million. Of this, £44 million would be covered by cost improvements in the NHS with the rest coming from the Reserve. The Reserve would therefore meet the great bulk of the excess cost. But the principle would have been established that the cost of the Review Body awards would not necessarily be met in full from the Reserve every year. As to teachers, the proposal was that the recommendations of the Interim Advisory Committee on School Teachers' Pay and Conditions (IAC) should be accepted in full. These were for a 6.3 per cent increase in the pay bill, with above-average increases for heads and deputies and in the value of incentive allowances. No extra funding should be provided to pay for this increase. Finally, it was proposed that the opportunity of next Session's Bill on Parliamentary Pensions should be used to remove the requirement for an Affirmative Order for increases in the Lord Chancellor's salary, which had provided the occasion for debate on the TSRB report generally. If the Cabinet agreed, she would announce the decisions on the Review Bodies that afternoon. A draft was attached as Annex A to C(89)4. At the same time, the Secretary of State for Education and Science would announce in the same way the decisions on the IAC recommendations. A draft of this Annex was attached as Annex B to the paper.

In discussion the following main points were made.

- a. The Review Body awards did not this year raise major difficulties. There might however be questions about the proposal that the NHS should bear a part of the excess cost of the awards for its groups. There was a very strong case for this proposal. Last year the excess cost to the NHS had been funded in full from the Reserve, and the presumption must not be established that this would happen every year. In presentation it should be emphasised

that, of the £248 million excess cost, over £200 million would come from the Reserve.

b. Last year an argument for meeting the excess cost in full from the Reserve was that the Health Authorities had already drawn up budgets assuming that no excess cost would fall on them. This argument no longer applied, since the Review Bodies' timetable had been brought forward so that decisions were made before the Authorities had completed their budgets. The draft Answer might be amended to refer to the new timetable.

The draft Answer said that the increase in provision for the NHS in 1989-90 over 1988-89 would be £1,899 million (a figure better rounded to £1,900 million). Larger figures had already been given publicly for the increase in funds available to the NHS, which took account also of a reduction in superannuation contributions, higher revenue, and cost improvements. The Answer should also give a figure on this basis.

d. There might be questions about the decision that local authorities would not receive extra grant to finance the IAC's recommendations, but these should not be difficult to deal with. Local authorities would benefit from a larger than expected reduction in employers' contributions to the superannuation of school teachers, and the unfunded gap would be only £32 million which was a very small figure in relation to local authorities' total expenditure on education.

THE PRIME MINISTER, summing up the discussion, said that the Cabinet endorsed the proposals set out in C(89)4. She would announce the decision on the Review Bodies, and the Secretary of State for Education and Science would announce the decision on the IAC, by Written Answer that afternoon. The Answer on the Review Bodies would be along the lines of Annex A to C(89)4, amended to take account of the points made in discussion and any drafting points. It was important that all the reports should be available to Members as soon as the Answers were given and that full briefing should be ready for Ministers and backbenchers.

The Cabinet -

Took note, with approval, of the Prime Minister's summing up of their discussion and noted that the Prime Minister and the Secretary of State for Education and Science would announce the Government's decisions accordingly.

ECONOMIC  
STRATEGY

6. The Cabinet considered a memorandum by the Chancellor of the Exchequer (C(89)3) on economic strategy.

THE CHANCELLOR OF THE EXCHEQUER introduced a discussion of the economic strategy, as a background to the Budget on 14 March.

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THE PRIME MINISTER, summing up the discussion, said that the Cabinet endorsed the approach to economic strategy set out by the Chancellor of the Exchequer in C(89)3. In particular they re-affirmed the central objective of bringing down inflation and agreed that economic policy should remain prudent and cautious.

The Cabinet -

1. Took note, with approval, of the Prime Minister's summing up of their discussion.

2. Invited the Chancellor of the Exchequer to take account of the discussion in preparing his budget.

Cabinet Office

16 February 1989

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# SUBJECT

MOST CONFIDENTIAL RECORD

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MOST CONFIDENTIAL RECORD  
TO  
CC(89) 6th Conclusions

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ECONOMIC  
STRATEGY

The Cabinet considered a memorandum by the Chancellor of the Exchequer (C(89)3) on economic strategy.

THE CHANCELLOR OF THE EXCHEQUER said that the past year had had both good features and bad. The good features had been rapid investment-led growth; a sharp fall in unemployment; the fastest growth of manufacturing productivity in any major nation; and profitability in the company sector at its highest level for twenty-five years. But there had also been an increase in domestic demand exceeding the capacity of the economy to meet it. Another way of expressing it was that total savings had remained constant, with a rise in company savings offsetting a fall in personal savings, while investment had gone up. This would take time to correct. It had been reflected in a substantial current account deficit, but the major problem had been the growth of inflation, although its extent was exaggerated by the inclusion of mortgage interest in the Retail Price Index.

Continuing, THE CHANCELLOR OF THE EXCHEQUER said that the problem of excess demand had been dealt with by a rise in interest rates. This was already starting to affect the housing market, retail sales and the growth of narrow money, although inflation was likely to go on rising for a few months. There were good signs therefore that the policy was working. But interest rates would have to remain high until it was quite clear that inflation was coming down. Indeed, if more needed to be done to control inflation, it would be done. Although monetary policy was the key to reducing inflation, fiscal policy must support it. A prudent and cautious fiscal stance was therefore essential. This indicated another sizeable Public Sector Debt Repayment during the coming year. The scope for tax reduction might well be largely restricted to offsetting fiscal drag, and any tax reform would have to be accommodated within this tight constraint. A difficult year lay ahead. The growth of the economy, and with it the decline in unemployment, must slow. It would be a few months yet before the inflation figure started to come down. But the prospects thereafter were good so long as the Government maintained its policy.

In discussion the following main points were made:

- a. The underlying economic position was strong but there was considerable evidence of the resurgence of inflation, for example in the construction industry. A revival of inflationary expectations could be extremely damaging. The need for prudence in framing the Budget was paramount.
- b. The increase in interest rates had so far had less political impact than might have been expected. The reasons for this might be that real earnings had continued to increase, that interest rates had only gone back to the level prevailing in the quite

recent past, and that savers, especially the elderly, benefitted from higher rates. Nevertheless, the possibility had to be allowed for that general public reaction might now become much sharper, especially among groups, like recent house buyers on low incomes, who were being especially hard hit. It was relevant that the full effect of the rise in rates had not yet been felt by borrowers with endowment mortgages from Building Societies which adjusted their rates only annually. Farmers also felt interest rates acutely, having suffered a fall in real income. It could be argued that, to the extent that tax reductions and interest rate reductions were alternatives, it was better to choose the latter.

c. A decision to make only small tax reductions when the Government had such a large Budget surplus would require careful presentation. More could be done to emphasise the advantages of debt repayment, which would be readily appreciated by the public at large.

d. There were some disturbing signs that retail sales, for instance of motor vehicles, were not responding to the tightening of monetary conditions. Indeed, since interest payments were often not separately identified in retail transactions, it was not clear how effective increases in interest rates were in this area. Moreover, banks, with foreign deposits encouraged by high interest rates in this country, were putting considerable effort into encouraging more borrowing. In the light of this, prospects for the balance of payments and inflation were bound to give cause for concern. On the other hand, some other indicators of retail sales, overseas holiday bookings and house prices indicated a response to the measures taken.

e. Table 2 in Annex 3 to C(89)3 showed that since 1979 Income Tax and National Insurance Contributions (NICs) had risen as a percentage of earnings for those on half average earnings. There was therefore a very strong case for concentrating on the lower paid the benefit of any tax reductions that fiscal policy allowed. This could most readily be done by raising the tax threshold rather than reducing the basic rate. Generally, action on the threshold was very attractive, although it could be argued that recent changes in the benefit system had reduced its impact on incentives. Another possibility was action on NICs, for example to raise the starting-point and improve the transition to the higher rates.

f. Other attractive possibilities for the use of any fiscal surplus that was available were: abolition of the pensioners' earnings rule, to encourage pensioners to stay in, or return to, the labour market; further concessions on lead-free petrol; under-indexation of the duty on petrol; and further action to encourage savings, perhaps by allowing tax relief on the initial investment. It would be important to take the opportunity of future privatisations to spread share ownership.

THE PRIME MINISTER, summing up the discussion, said that the Cabinet endorsed the approach to economic strategy set out by the Chancellor of the Exchequer in C(89)3. In particular, they agreed on the need to give priority to countering inflation and on the case for a cautious fiscal policy. They also believed that any tax reductions that were possible should bring particular benefit to the lower paid.

The Cabinet -

1. Took note, with approval, of the Prime Minister's summing up of their discussion.
2. Invited the Chancellor of the Exchequer to take account of the discussion in preparing his Budget.

Cabinet Office

17 February 1989