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10 DOWNING STREET

From the Private Secretary

10 February, 1982.

Sir Raymond Pennock and Sir Terence Beckett came in for a meeting with the Prime Minister yesterday evening.

Sir Raymond Pennock thanked the Prime Minister for finding time to see them. They wished to reiterate and to enlarge upon certain aspect of the budget representations which they had made to the Chancellor. The CBI's hope was that the budget would be a businessman's budget. The economy was undoubtedly picking up; they hoped that the budget would add some impetus to the increase in activity. The measures they had in mind would take some while to have an effect, and they thought i important that there should be a budget framed to help business this year rather than next when the election would be too close for the effects to have their maximum impact.

Sir Terence Beckett said that the industrial scene was in a much healthier state this year than when they had made their representations 12 months ago. There had been a spectacular growth in output per person. If industry could get its output back to a 1979 level there would be a very large increase in its profitability. The pay round was going well, with the vast majority of settlements in the 4-6% range. On exports, volume at the end of last year was 7% higher than 12 months earlier. Industry felt that it was doing its stuff; but it was still burdened by heavy costs from the public sector. Of these the National Insurance Surcharge was highly onerous. Sir Raymond said that this cost his company £9 million last year, some 10% of their profits. He assured the Prime Minister that if they were relieved of this burden, £9 million more would go into new investment and new technology. None of it would go into wages. Industry was still suffering very high local authority rates; and energy costs were still much too high, especially for electricity.

Sir Raymond Pennock said that they hoped that the Prime Minister would not take too much account of what the CBI had said in its budget representations about the size of the PSBR. Their economists had suggested this figure, and all concerned recognised the extent to which uncertainty clouded these matters. The CBI's concern was a practical one - that the budget should be good for business.

Sir Terence Beckett said that the CBI's proposal for an addition of £1.8 billion to the PSBR had been criticised by many of their members as being excessively modest. But he recognised that the take-off from the recession must be slow if we were to avoid bottlenecks and adding to inflationary pressures. At their meeting at the

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Treasury it had been argued that the CBI's proposals in relation to the NIS were too indiscriminate in their effect upon industry, and would leak into wages. They thought neither of these arguments was strong. It was their belief that companies would use this additional room for manoeuvre to improve their competitiveness and reduce their costs, and not to finance higher wage settlements. The effect on nationalised industries and local authorities could, they believed, be easily offset by corresponding reductions in EFLs and the RSG. They handed the Prime Minister a table to illustrate their contention that the benefit of the reduction they proposed would not be indiscriminate. Finally, they argued that the NIS is the reverse of an export subsidy: a reduction would improve the competitive position of our industries in relation to that of their overseas competitors.

The Prime Minister said that it was useful to hear the CBI's views at this stage. She reminded the CBI representatives of the savings to industry which had accrued from the shake-out of labour over the past two years. These costs, together with powerful political criticism, now fell upon the Government. The Prime Minister also noted that when the Government had announced increases in National Insurance contributions these had been framed asymmetrically, so as to minimise the additional burden upon industry. She pointed out that tax reliefs in the personal sector were also an important factor so far as the health of industry was concerned. This had been particularly importan for management. She was concerned lest the CBI set their sights too high, so that there would be a risk that a good and fair budget would be criticised because it did not come up to excessive and pre-conceived benchmarks. The Prime Minister said that financial markets had in this recession rumbled governments: they were not this time round prepared to see negative real interest rates as they had done after the first major oil price rise. But it was vital, particularly for small businesses, to keep interest rates as low as possible. We must ensure that our emergence from a recession should occur in a sound and sensibl way.

I am sending a copy of this letter to Jonathan Spencer (Department of Industry).

M. C. SCHOLAR

John Kerr, Esq.,
HM Treasury.