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10 DOWNING STREET

Prime Minister ² *DEW*
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This is an interesting
and rather surprising
piece by Patrick Minford.
The Chancellor should be
very grateful!

RS

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Has Lawson made a U-turn?

THERE has been a lot of holier than thou comment on Mr Lawson's Autumn Statement, when he announced around a £4.7 billion increase in the public expenditure total for 1987-88. On one side, those who have repeatedly urged him to spend more rather than cut taxes have accused him of a "disgraceful", nay "cynical", U-turn.

On the other, the hairshirt brigade, who disapprove of all spending private and public, castigate him for spending his burgeoning tax revenues on things the opinion polls suggest tax-payers want them spent on; he is, they say, stoking a runaway pre-election boom, which will be inflationary and so on.

The fact is that the wind of change is beginning to be felt in education, in the local government rates. No reforms can occur overnight in a society like Britain, where because rights are generally respected there is a deep conservatism.

More competition in the provision of education and more parent choice will require motivation and enthusiasm among good members of the teaching profession; just as privatisation has required the motivation of each industry's managers and workers. So it makes sense to invest in a more productive pay structure, as part of the reform process.

Similarly on unemployment, the Restart programme costs a bit. But, in a quiet way, without beating the drums of "workfare", this important reassertion of the original Beveridge system of incentives is getting more people back to work.

As for local government, again key reforms are on the way. For troubled areas like Merseyside, these reforms will be a lifeline; with business rates capped or unified, the local businessman will breathe again, and the militants will go into retreat as their supporters start to pay the community charge and so pay some of the bill for their irresponsibility.

All reforms need some sort of bridge into the future; they must cost a bit in the transition, because a political constituency for reform has to be created and existing rights in the old system have to be bought out.

Mrs Thatcher has a sound populist instinct; the recent Conservative party Conference emphasised radical changes as part of a popular programme of reform that would give power over their lives back to the people. If the people, meanwhile, are signalling that they do not want the existing structure to self-destruct while the changes are going through, they not only hold the whip hand; they are also being logical.

This reform programme—part of the ongoing step-by-step Thatcher process—holds the key to disciplining public expenditure in the long term. Paradoxically, I am much more optimistic now about future public expenditure trends than I have ever been before.

What then of tax cuts? With a £7 billion target for 1987-88, and if oil prices stay around \$15 a barrel, the Chancellor can probably find about £2 billion in tax cuts—enough to cut the standard rate to 27p.

However, it could be more than this as non-oil tax revenues are growing well over budget (12.5 p.c. this year and perhaps the same next); oil prices are still bumping around and the big tax gathering season is in the first quarter of 1987 so we will not really know until just before the Budget.

There would be a case for cutting taxes by more still and raising the PSBR if one could be absolutely confident about the course of future public expenditure reforms.

The objective of public sector borrowing is to allow tax rates to be set at a viable constant long run level, because constant tax rates give the private sector a firm basis on which to plan and no artificial incentive to defer or accelerate projects; this means a level that will pay for long public spending

and allow for possible expenditure "crises" (such as wars or large scale strikes).

The trouble is, of course, that, particularly at a time of radical change, there is no objective way of measuring this. Accordingly, the philosophy of the medium term financial strategy is suitably cautious; public sector borrowing is due to fall slowly as a fraction of GDP, implying a faster fall in the ratio of public sector debt to GDP. That way leaves room for future expenditure crises that may drive up debt.

Taxes are cut as the money comes in from actual reforms, breeding confidence that it will be there in the future. On this basis a £7 billion PSBR for 1987-88 looks about right.

I have not yet answered the hairshirt brigade; presumably they will be demanding higher taxes and higher interest rates soon on the grounds that demand is running away and must be cut back. This is illogical stuff; in fact, it is really just a recrudescence of Keynesian demand-management, only with a downward rather than an upward bias.

The role of the public sector is to set tax rates so as to balance its books over the long term; and to obey a proper monetary target, namely at present Mo (because of deregulation, bank credit proxies such as sterling M3 are quite misleading).

I suppose eventually, when they have had to consign another set of hopeless inflation forecasts to the incinerator, our City economists will come round to M0.

They point to "overheating" in the south east; but that overheating has a purpose. When it has driven more companies to relocate in the north it will be doing its proper job as part of the relative price mechanism. The idea that there is some sort of nationwide runaway boom deserves only hollow laughter.

Patrick Minford

Professor of Applied Economics at Liverpool University.

Suspension likely for Cambrian

DEALINGS in the shares of Cambrian & General Securities, Wall Street arbitrageur Ivan Boesky's United Kingdom investment trust vehicle are

Dutch back shopkeepers

By David Green in Amsterdam

THE DUTCH are coming to England with an idea in retailing which, they believe, will help the independent shopkeeper in his fight to prosper among the massed ranks of the multiples.

The concept, called Best Shops in Town, was launched

schedule is to sign up some 30 towns by the end of February and to begin television advertising in March. British retailers will be paying £1,750 a year.

In Holland 978 of the retailers have renewed their membership and Joss Bouben, Best Shops managing director, believes the

National Savings rise by £10m

NATIONAL Savings had its best cash inflow in October since March last year. The £533.1 million in receipts was