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10 DOWNING STREET

From the Private Secretary

3 January 1984

Dear John,

PUBLIC EXPENDITURE REVIEWS

The Prime Minister has seen the Chief Secretary's minute of 22 December and welcomes the effort to focus on key areas of public expenditure in order to identify options for savings to be followed up in the next Public Expenditure Survey.

The Prime Minister agrees that the objectives of the urban programme need to be clarified and ways of measuring its cost-effectiveness need to be developed. She would be grateful if the Chief Secretary would approach the Secretary of State for the Environment and other colleagues to set such a review in hand.

On defence equipment expenditure, the Prime Minister is still considering how best to handle further work in this area.

The Prime Minister is very concerned about the growth of expenditure on the Family Practitioner Services and she would therefore welcome the proposed review of the contractual relationship between the NHS and the contractor professions. She is also concerned about the current growth of social security expenditure, as recorded in the Chief Secretary's letter to the Secretary of State for Social Services of 22 December. She is particularly concerned about the growth of housing benefit and in addition to work on forecasting and control she is anxious to establish why housing benefit has become so widespread, extending a long way up the income scale. In particular, she would like to know how current expenditure on housing benefit compares with the forecasts which were made at the time this new benefit was established. In both these areas, she would be grateful if the Chief Secretary would approach the Secretary of State for Social Services to set in hand the work required. A preliminary discussion of these issues is likely to take place in the meeting arranged for 12 January.

On territorial programmes, the Prime Minister has noted the argument that overall spending, in relation to "needs", in Scotland and Northern Ireland is substantially higher than in England and Wales. Before deciding how best to approach the other Secretaries of State, the Prime Minister would be interested to see a summary of the work which the Treasury has undertaken.

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In all of these areas, the Prime Minister would be grateful if the No.10 Policy Unit could be kept closely involved.

Yours sincerely

Andrew Turnbull

Andrew Turnbull

John Gieve, Esq.,
Chief Secretary's Office.

The Autumn Statement: A Summary

The Chancellor of the Exchequer presented his *Autumn Statement* to Parliament on 17 November 1983. This Supplement summarises the *Statement*, which is published in full as House of Commons Paper 112 (HMSO £4).

THE FORECAST IN OUTLINE

Output, demand and employment
In the UK output has been rising since 1981, as real domestic demand has recovered, helped by falls in inflation and interest rates. Output in 1983 is expected to be about 3 per cent higher than in 1982. The growth in domestic demand is likely to slow down perhaps from 4 per cent in 1983 to 3 per cent in 1984, but a continued rise in investment and a recovery in exports should sustain the growth in activity. With world demand recovering, and the profitability of home supply increasing, the forecast is for UK output to grow by 3 per cent in 1984 and for employment to rise.

Balance of payments
The main factor in the sharper growth of imports relative to exports since 1981 has been the recovery in domestic demand in the UK, ahead of most other industrial countries. This has been reflected in the current account of the balance of payments, where a surplus of over £5 billion in 1982 has given way to a small surplus in the first nine months of 1983. With a recovery forecast for exports, the current account may remain near balance in 1984. The forecast assumes that the exchange rate will not change much from recent levels.

Inflation
This year has again seen a lower than expected rate of inflation in the UK. Costs are rising more slowly than prices, leaving room for a sizeable recovery in profitability from an historically low base. At the same time the real income of those in work has risen. Current inflationary pressures continue weak and by the end of next year inflation should be below the current rate of about 5 per cent.

Borrowing
The public sector borrowing requirement in this financial year, 1983–84, looks like turning out higher than expected at Budget time. This is despite the 7 July measures and partly reflects the same factors that caused higher than expected spending at the end of 1982–83. For 1984–85, this forecast continues to assume, as in the medium-term financial strategy, a public sector borrowing requirement of 2½ per cent of gross domestic product, or £8 billion. The present forecast, subject to a wide margin of error, assumes an increase of taxation in order to achieve this, after allowance for indexation of personal taxes and specific duties.

Monetary policy
Monetary policy in 1984–85 is assumed, like fiscal policy, to be consistent with the indications given in the medium-term financial strategy. These included a range for monetary growth of 6–10 per cent.

World economy
A vigorous rise in activity in the US is not being matched elsewhere. In parts of Europe, in OPEC, and in many of the developing countries, activity and imports have fallen, in the process of adjustment to international or national debt problems. World trade is only now beginning to recover after the fall of the last two years.

ECONOMIC PROSPECTS FOR 1984

The world economy

Recent developments
Output rose in all the major countries in the first half of 1983. Rapid growth in the US continued into the third quarter, but the recovery in Europe has been weak and erratic. Underlying inflation in the major six economies has fallen to about 5 per cent. Interest rates in most countries remain high in real terms. The upward trend to unemployment has slowed substantially in many countries, and is being reversed in the US.

After falling substantially during 1982 world trade in manufactures appears to be growing again in the course of this year, largely as a result of the growth of imports into the US. Many developing countries, including some members of OPEC, have had to reduce imports sharply because of falls in their earnings from primary products and because of difficulties in meeting debt obligations or obtaining fresh bank credit. Oil prices fell earlier this year in the face of a substantial fall in demand but other commodity prices have been rising from very low levels in 1982.

Prospects
Recovery in the US is expected to moderate after the rapid growth in mid-1983. In Europe recovery should resume in 1984 after some faltering in the second half of this year. Inflation, overall, may not change much, with a slight rise in the US matched by further falls in Europe. Outside the OECD area, the timing and extent of recovery in imports, as the need lessens for further downward adjustment, is very uncertain. On the assumption of improved export earnings and financial flows, developing countries should be able to sustain renewed growth in imports in 1984. The recovery in world trade should be faster than that in output; this is the normal pattern in an

Table 1 World economy

	Percentage changes on a year earlier				
	Average 1975–82	1981	1982	1983	1984
GNP(1)	3	2	−½	2½	3½
Prices(1) (consumers' expenditure deflator)	8½	9	7	5	5
World trade in manufactures (weighted by UK markets)	4	3½	−3	−1	5

(1) Major six countries (US, Japan, Germany, France, Italy, Canada).

upswing of the cycle, but seems not to have occurred in 1983 because of sizeable falls in imports in many countries outside the major six. The outlook for the world economy is summarised in table 1.

Exchange rate, relative costs and trade

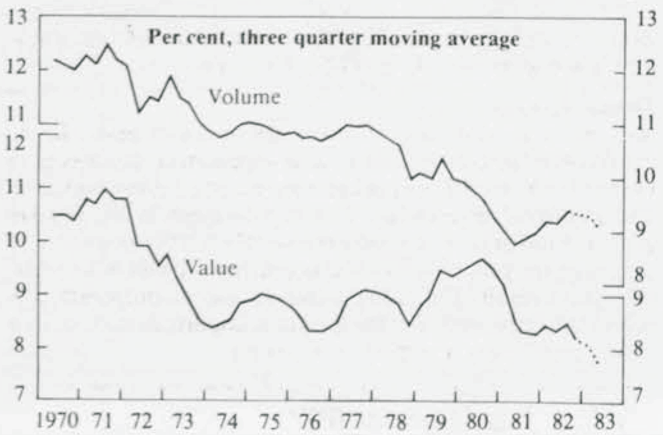
Relative costs

Over the course of the last two and a half years there has been a partial reversal of the sharp deterioration in relative costs in the 1978–81 period. Between the first halves of 1981 and 1983 the level of domestic unit labour costs in manufacturing relative to those of our competitors is estimated to have fallen 20 per cent. This was rather more than the fall in the effective exchange rate: above-average productivity gains, and reductions in the national insurance surcharge, partly offset by slightly higher earnings growth in the UK, resulted in domestic costs in manufacturing rising slightly less than those of our competitors. For the purposes of this forecast it is assumed that the effective exchange rate will not change much from the average level for the first three quarters of 1983. Further gains in relative costs are likely to depend on improvements in UK unit labour costs relative to those overseas.

Trends in trade

Over the course of the 1970s and early 1980s a number of structural changes have been taking place in the UK economy. These have been reflected in the diverse movements of the components of the visible trade balance. The surplus on non-manufactured goods has been on a rising trend, and the balance of trade in oil has moved from a deficit of 3 per cent of nominal GDP in 1976 to a surplus of 1½ per cent last year. But the balance of trade in manufactures, as a percentage of nominal GDP, has shown a falling trend over this period. Trends in shares of UK exports in world trade manufacturing are shown in chart 1.

Chart 1 Shares of UK exports in world trade in manufacturing



Due to an error in rebasing the volume series to 1980 prices, this chart as published in the *Autumn Statement* (no. 1.4) contained incorrect figures for the volume share of UK exports of manufactures in world trade between 1974 and 1977.

Trends in import penetration have varied by sector. Outside manufacturing there has been no general upward trend, with falls in some sectors. Within manufacturing, import penetration has risen strongly.

For 1983 as a whole, the volume of total exports is expected to be slightly higher than in 1982. While the level of exports of manufactures has been a little weaker than expected at Budget time, reflecting the lower level of world trade in 1983, oil exports have been rather higher. The rise in imports of manufactures, perhaps 10 per cent or more in 1983, results in roughly equal measure from both the rapid growth in the domestic demand for manufactures and a further loss by UK manufacturers of share in the domestic market. Imports of basic materials have also risen this year with the recovery in domestic activity, although imports of fuel and services have tended to fall. Imports of goods and services in volume terms could be 5 per cent higher than in 1982.

Trade prospects

Recovery in the world economy and recent improvements in UK competitiveness should lead to a period of growth in export volumes. This would be consistent with recent evidence from the CBI survey, where there is a positive balance of respondents optimistic about export prospects. With North Sea oil production approaching its peak, exports of fuels are expected to be broadly unchanged from recent levels. Exports of manufactures, non-manufactured goods and services are all projected to increase. Further growth in import volumes of manufactures is likely in 1984, as the economy continues to expand, although import volumes for non-manufactures, including fuel, may change little from current levels.

Terms of trade

So far there has been only a small deterioration in the non-oil terms of trade since the peak in 1981. Some slight further fall is expected, as importers raise prices to cover higher costs, including higher commodity prices. Exporters' profit margins should continue to recover.

Current balance

Between 1981 and the first nine months of 1983, the current account of the balance of payments moved from a surplus of £6½ billion to a position of small surplus. Much of this change reflected the earlier recovery in UK demand compared with the rest of the world. But the recovery of world trade now expected for 1984 should lead to growth in exports much more in line with growth in imports. With an increase in the invisibles balance, on services and interest, profits and dividends, the prospect is for broad balance in the current account over the forecast period.

Inflation

As expected, the 12-monthly increase in the retail prices index has turned up in recent months, from a low of 3¾ per cent in May and June to 5 per cent in October. This upturn mainly reflects the particularly favourable profile of retail prices in the second half of last year and early 1983 and it is expected to be only temporary. Underlying inflationary pressures remain downward with producer prices for home sales of manufacturing output increasing by 5½ per cent in the year to October compared with 7 per cent a year ago.

The market price GDP deflator rose by 5 per cent in the year to the second quarter of 1983 (6½ per cent in the financial year 1982–83) compared with 15 per cent at the beginning of 1981. This reflected much smaller rates of increase in the main elements of domestic costs as financial and competitive pressures on industry encouraged lower pay settlements and historically exceptional gains in manufacturing productivity. In the first half of 1983, unit labour costs in the whole economy were only 2 per cent higher than a year earlier, with the reductions in the national insurance surcharge helping to limit the growth in industrial costs. Profit margins, squeezed severely in many sectors during the downturn, have been recovering since 1981.

Costs

World inflation rates have also declined appreciably over the last two years, with commodity prices falling through most of 1982. Although some commodities have recovered strongly this year, the effect on the UK economy has been fairly muted. While the spot market rates which enter into some of the most widely-quoted indices of commodity prices have risen rapidly, there has been less impact on the prices at which most trading has actually taken place. Oil prices have also been fairly steady since the fall early in 1983. Import prices, though rising faster than domestic costs, have not provided strong upward pressure on prices charged by domestic producers.

Pay

Pay settlements in the year ending in August were fairly tightly bunched around an average level of about 5½ per cent. Little variation was observable in settlements as the round progressed. Because of productivity bargaining, grading drift and other factors, earnings growth is usually above settlements and was about 7½ per cent during the last pay round. This was about 1½ per cent less than in the previous year but the

slowdown in earnings growth did not match that of prices. In August 1982, retail prices had been 8 per cent above the level of a year earlier. By the end of the pay round retail prices were rising at only 4–5 per cent. With wage-earners also benefiting from the increases in tax allowances in the 1983 Budget, after-tax real earnings for an average employee rose about 4 per cent during the year to August 1983.

At the same time, employers' labour costs per unit of output – held down by substantial gains in productivity and the reductions in national insurance surcharge – were rising more slowly than prices being charged by producers. The past year has therefore seen both rising real earnings and falling real unit labour costs.

Prospects

The current pay round is starting against an improved background for both employees and employers with real take-home pay higher and unit labour costs rising more slowly than prices. Competitive pressures are still strong, both on employers in world and domestic markets and on employees in a weak labour market. So, despite the continued recovery in domestic output and a rise in employment over the next year, there should not be a reversal of the downward trend of earnings growth.

Lower rates of inflation now being achieved in other industrial countries are reinforcing the pressures on domestic industry to keep down prices and costs. Over the next year, allowing for some further recovery in margins, the market-price GDP deflator is expected to rise by about 5 per cent. Taking account of movements in import prices and the recent bumpy path, annual changes in the retail prices index may be a little more volatile. Some further increase – perhaps to about 5½ per cent – is expected for the 12-monthly rate in the first half of next year as past favourable factors drop out of the comparison. These effects should, however, be short-lived and the 12-monthly increase is expected to fall back, perhaps to around 4½ per cent by the end of 1984.

Domestic recovery and a rise in external demand, with prices tending to rise faster than costs in most markets, will all contribute to a continuing rise in profits. While profitability for most industrial and commercial companies, outside the North Sea, is not yet back to 1979 levels, there has already been a sizeable recovery since 1981, reflected in a larger financial surplus as the rise in company expenditure has not fully kept pace with the rise in income.

Demand and activity

The base year for constant-price estimates of output and expenditure was changed this summer from 1975 to 1980. The direct effect of rebasing on year-to-year GDP changes was probably fairly small, but it combined with the usual process of revision as a result of new information to produce a different pattern of GDP growth over the past five years. The fall in GDP in 1981 was smaller than had been thought and the recovery since the trough of the recession has been faster as shown by the average of the expenditure, income and output measures.

Output growth

Latest estimates put the growth of the average measure of GDP between the first halves of 1982 and 1983 at nearly 3 per cent. Within this average the expenditure measure showed a growth of over 3½ per cent while the output measure (conceptually identical, but compiled largely from independent data sources) showed a rise of nearly 2 per cent. Although the output measure is generally preferred as a guide to shorter-term, particularly within-year, movements, the average measure is usually more reliable for longer periods and provides the main basis for the assessment of activity movements in this forecast.

The buoyancy of GDP over the past year has reflected recovery in domestic demand. Consumers' expenditure, which had been virtually flat over the previous three years, rose by 3 per cent in the second half of 1982 and a further 1½ per cent in the first half of 1983. Fixed investment, particularly in dwellings, is recovering.

Personal consumption

Since the first half of 1982 real personal disposable income, in total, has been little changed. The rise in consumers' expenditure (and the fall in the saving ratio from over 12 per cent in the first half of 1982 to over 8½ per cent in the first half of 1983) has been mainly financed by a rise in borrowing. Lower inflation and lower interest rates have been major factors in the fall in saving: lower inflation has meant that consumers have needed to save less to maintain the real value of their financial wealth. In the 1960s, when inflation averaged 4 per cent, the saving ratio averaged 8 per cent.

Total real personal disposable income is now beginning to rise again as real take-home pay rises and employment stops falling. But other factors bringing about a lower saving ratio – primarily lower inflation and nominal interest rates – should continue to have an impact. The fast growth recently experienced in consumer durables expenditure (20 per cent over the last year) is not expected to continue, but the saving ratio is expected to stay below last year's level as expenditure on non-durables recovers further. The rise forecast for consumers' expenditure in 1984 reflects both a small further fall in saving and a rise in real after-tax incomes.

Investment

Total fixed investment, which fell in 1980 and 1981, rose in 1982, and in the first half of 1983 was nearly 3 per cent up (at constant prices) on a year earlier. Two areas of private fixed investment – house-building and investment by manufacturing industry – fell sharply in the recession. Outside manufacturing, business investment now seems to be growing at an annual rate of some 6 per cent.

Surveys point to a steady growth in industrial investment, including manufacturing investment, in 1984, reflecting recent and prospective rises in output and profits. Total fixed investment is forecast to rise by 4 per cent in 1984.

The improvement in prospects for industrial investment reflects in part the better financial position of the company sector as margins as well as output recover. This is also expected to relieve some of the pressure on stock levels. Much of the destocking in 1980 and 1981 reflected companies' need to improve their cash flow at a time of high interest rates and poor output expectations. Recent surveys suggest that, with expectations of output growth fairly stable, stock–output ratios may not depart radically from current levels.

Demand and activity

As the UK and world recoveries become more firmly established the composition of final expenditure is expected to begin to shift away from personal consumption towards exports and industrial investment. The improvement in the relative cost position of domestic industry over the last two years should also limit the proportion of additional demand met by imports, though, overall, the rising trend in import propensities is forecast to continue. But the growth in imports should be more nearly matched by the growth in exports.

Table 2 Expenditure and GDP

Percentage increases on a year earlier

	1982	1983	1984
Domestic demand[1]	3	4	3
Exports of goods and services[1]	1½	½	4
Imports of goods and services[1]	3	5	5
Domestic production – GDP at factor cost (average measure)	2	3	3

[1] Expenditure measures at market prices.

Table 3 Output

1980=100

	1983		1984	
	I	II	I	II
GDP (average measure)	102½	103½	105	106½
Manufacturing output	94½	95½	97	98

Manufacturing output resumed its slow recovery at the beginning of 1983 and latest data suggest that the level of output in mid-year was about 3 per cent above the trough of the first quarter of 1981. In the same period, the average measure of GDP rose by about 5 per cent. With the expected recovery in exports and fixed investment, the growth in manufacturing production in 1984 may not be very different from that of the economy as a whole.

Productivity and the labour market

Most productivity gains made over the last three years have been in the manufacturing sector. Since the end of 1980, employment in manufacturing has fallen by one million or 15 per cent while output has not changed very much. The rise of over 18 per cent in output per person employed in the manufacturing sector has been the major factor in the 10 per cent increase in output per head in the whole economy. As output growth is being consolidated, so the fall in employment seems to be ending; manufacturing employment (which now accounts for about one quarter of total employment) has been declining more slowly in the last six months while outside manufacturing, employment is now rising. Unemployment may now be levelling off. Other labour market indicators, notably unfilled vacancies and hours worked, are pointing to some recovery in the pressure of demand for labour.

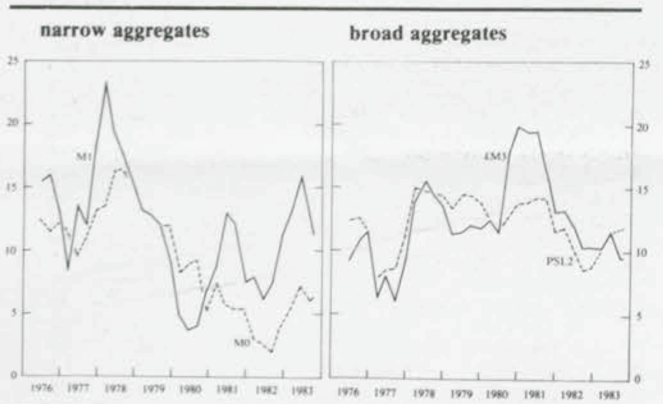
Monetary growth and fiscal projections

Money supply and interest rates

US interest rates, which had fallen rapidly during 1982, rose a little in 1983, in response to the rapid recovery in activity and to the faster rise in monetary aggregates. In the other major OECD economies, there was no significant change in interest rates.

In the current target period, February 1983 to April 1984, the growth of £M3 to mid-October was just within the target range of 7–11 per cent. PSL2 and M1 were rather above the top of the range. Since the summer, monetary growth on all three measures has slowed significantly compared with earlier in the target period. Narrower non-interest-bearing forms of money continue to grow more slowly than the broader aggregates. The forecast makes the same assumption about 1984–85 as the medium-term financial strategy: that there will be a range for M1, £M3 and PSL2 of 6–10 per cent. (See *Economic Progress Report,* December 1983, for article on monetary aggregates.)

Chart 2 Monetary growth, percentage changes on a year earlier
for banking months March, June, September and December



Fiscal projections

The public sector borrowing requirement in 1982–83 was £1½ billion higher than forecast in the *Financial Statement and Budget Report.* There was less underspending on central government voted expenditure and higher borrowing by local authorities. The higher level of central government expenditure and higher local authority borrowing seems to have continued into the current financial year. This explains a substantial part of the upward revisions to the anticipated level of public expenditure and the public sector borrowing requirement in 1983–84, despite the cash limit reductions and additional asset sales announced on 7 July. In the first seven months of 1983–84, the public sector borrowing requirement was just over £7 billion. The total for the year as a whole is now projected at £10 billion, some £2 billion higher than forecast at Budget time. There is inevitably still a substantial margin of error surrounding this forecast (average errors in public sector borrowing requirement forecasts at this time of year exceed £2 billion) but there are several factors which give grounds for expecting increased public borrowing this year. On the expenditure side the outturn for 1982–83 and information on likely spending this year suggest less shortfall than allowed for in the *Financial Statement and Budget Report.* In addition, debt interest payments are higher, partly because of higher borrowing. On revenues, extra receipts from North Sea oil seem likely to be broadly offset by lower receipts elsewhere.

Adopting the conventional assumptions of indexed tax rates, allowances and specific duties and taking a public sector borrowing requirement in 1984–85 of 2½ per cent of GDP, equivalent to £8 billion (as in the medium-term financial strategy), this points to a negative fiscal adjustment, perhaps of the order of £½ billion. The forecast assumes, conventionally, that the fiscal adjustment takes the form of an increase in income tax. The size of the fiscal adjustment is, of course, extremely uncertain and depends on revenue and expenditure estimates subject to a number of major uncertainties, in either direction. For the public sector as a whole, the flows on either side of the account approach £200 billion.

General government expenditure in national accounts terms is forecast to rise, in cash, nearly 5½ per cent in both 1983–84 and 1984–1985. Table 4 shows the basis of these figures.

Table 4 General government expenditure[1]

	1982–83	1983–84	1984–85
			£ billion
General government expenditure[2]	114	120½	126½
National accounts adjustments[3]	3½	4	5
Interest payments	14	14½	15
Total expenditure in national account terms	**132**	**139**	**146½**

[1] Totals may not add due to rounding.
[2] Expenditure on programmes by central government and local authorities plus the contingency reserve and special sales of assets, after making allowance for expected outturn.
[3] Adjustments to line 1 to the definitions used in national accounts statistics.

Revenue

Revenue estimates depend on incomes, spending and prices, as well as on policy decisions. Revenue in 1984–85 is projected on conventional assumptions of revalorisation of the main direct tax allowances and thresholds, and of excise duties, using a figure of 5 per cent. Estimates for oil revenues assume that North Sea oil prices do not change very much from present levels.

The revenue projections are shown in table 5. Real GPD (average measure) is forecast to grow by nearly 3 per cent in 1983–84 and 1984–85. The general rate of inflation, as measured by the GDP deflator, is put at about 5 per cent in 1983–84 and 1984–85.

PUBLIC EXPENDITURE IN 1984–85: THE GOVERNMENT'S PLAN IN OUTLINE

Plans for public expenditure in 1984–85, as set out in the last public expenditure white paper (PEWP)*, have been revised and new outline plans set out in the *Autumn Statement.* Full figures will appear in the next PEWP shortly before the Budget. All figures are in cash unless otherwise stated.

The planning total for 1984–85 has been held to £126.4 billion in line with figures given in the 1983 PEWP.

Planning total figures for each year since 1978–79 in cash and in 'cost terms' are shown in table 8 (cost terms – this is at 1982–83 cost as measured by the GDP deflator, a wider annual index of changes in total home costs than the RPI). The table also shows how public expenditure has fallen as a percentage of gross domestic product (GDP) from 44 per cent in 1981–82 to a planned 42 per cent for 1984–85.

**The Government's Expenditure Plans 1983–84 to 1985–86* Cmnd 8789.

Revised spending plans for 1984–85 are compared with the last white paper figures after Budget and other modifications in table 10.

Although the planning total remains unchanged there have been alterations to individual programmes. Increases, mainly in demand-led programmes, e.g. pension payments, have been offset by savings elsewhere and there has been an increase of £0.4 million in estimated receipts from special sales of assets reflecting the expected sale of Enterprise Oil (see *Special sales of assets* below) and other factors.

Table 5 General government receipts[1]

	1982–83	1983–84	1984–85
			£ billion
Taxes on income, expenditure and capital	92	96	104
National insurance and other contributions	18½	21	22½
Interest and other receipts	11	11	11
Accruals adjustments	—	—	—
Total receipts	**122**	**128**	**137½**
of which North Sea tax revenues	8	9	9½

[1] Totals may not add due to rounding.

Table 6 Public sector borrowing

	1982–83	1983–84	1984–85
			£ billion
General government expenditure	132	139	146½
General government receipts	−122	−128	−137½
Implied fiscal adjustment[1]	—	—	−½
General government borrowing requirement	10½	11	8½
Public sector borrowing requirement	9	10	8
as percentage of GDP	3¼	3¼	2½
Money GDP at market prices	282	305	329

[1] On the same assumption as in the 1983 MTFS about the PSBR as a proportion of GDP.

Table 7 Economic prospects[1]

	1982 to 1983	1983 to 1984	Average errors[2] from past forecasts
			Percentage changes
A Output and expenditure at constant 1980 prices			
Gross domestic product (at factor cost)	3	3	1
Consumers' expenditure	3½	2½	1
General government current expenditure	2½	1	1½
Fixed investment	2½	4	2½
Exports of goods and services	½	4	3
Change in rate of stock-building as a percentage of the level of GDP	1	½	1
Imports of goods and services	5	5	3
	1983	1984	
B Balance of payments on current account (£ billion)	½	0	3
C Retail prices index (4th quarter)	5	4½	3[3]

[1] The forecast includes the effect of the fiscal adjustment in 1984–85.
[2] The errors relate to the average differences (on either side of the central figure) between forecast and outturn. The method of calculating these errors has been explained in earlier publications on Government forecasts, notably in the *Economic Progress Report*, June 1981. The errors are after adjustment for the effects of major changes in fiscal policy, which excluded from the forecast.
[3] The average error for inflation was calculated from a period of much higher inflation and probably overstates the margin of error at low rates of inflation.

Table 8 Public expenditure planning totals 1978–79 to 1984–85

	Cash[1]	Cost terms[1,2] base year 1982–83	Public[3] expenditure as % of GDP
	Planning total £ million		
1978–79[4]	65 800	106 800	40½
1979–80[4]	76 900	107 800	40½
1980–81[4]	92 700	108 600	42½
1981–82[4]	104 600	111 600	44
1982–83[4]	113 400	113 400	43½
1983–84[5]	119 800	114 100	42½
1984–85[5]	126 400	114 600	42

[1] Figures are rounded to the nearest £100 million.
[2] Cash plans adjusted for general inflation as measured by the GDP deflator at market prices. The GDP deflator is forecast to increase by some 5 per cent in 1983–84 and some 5 per cent in 1984–85.
[3] Includes planning total plus net debt interest, payments of VAT by local authorities and non-trading government capital consumption.
[4] Outturn/estimated outturn.
[5] Plans.

Special sales of assets

Net proceeds from special sales of assets are shown as increasing by £400 million, reflecting a number of changes, including the postponement of the sale of Enterprise Oil (the company has been set up to take over the oil assets of British Gas) from 1983–84 to 1984–85. There are considerable uncertainties attached to this figure, which is dependent on market conditions at the time of sales.

Nationalised industries

External financing limits (EFLs) – made up of grants by government plus nationalised industries' net borrowing in a financial year – for nationalised industries in 1984–85 are set out in table 9. Overall, there is a decrease of £666 million in expected external financing requirements. Requirements have decreased for all industries, except the National Coal Board, the British Steel Corporation, British Shipbuilders and the Civil Aviation Authority.

Table 9 External financing limits for the nationalised industries (1984–85)

	£ million[1]
National Coal Board	1 103
Electricity (England and Wales)	−740
North of Scotland Hydro-Electric Board	−2
South of Scotland Electricity Board	261
British Gas Corporation	−100
British Steel Corporation	275
British Telecom	−250
Post Office	−52
National Girobank	−1
British Airways Board	−160
British Airports Authority	10
British Railways Board	936
British Waterways Board	43
National Bus Company	66
Scottish Transport Group	16
British National Oil Corporation[2]	−4
British Shipbuilders[3]	175
Civil Aviation Authority	20
Water (England and Wales)	286
Total	**1882**

[1] Figures are shown rounded to the nearest £1 million.
[2] The figure for BNOC is not a limit. BNOC's trading results are likely to fluctuate from year to year given the uncertainties of oil trading.
[3] The British Shipbuilders EFL is provisional pending decisions on the industry's corporate plan.

Reserve

The white paper included for 1984–85 a provisional reserve of £3 billion. In the 1983 review of plans no call has been made on this reserve, which will be available to meet all contingencies including estimating changes.

Education and Science
Provision is increased by £175 million overall. Four-fifths of the programme is local authority current expenditure. Within other expenditure there is increased provision for the costs of subscriptions to international science; an increase, after higher parental contributions and other savings, in provision for awards for more students in higher education; and savings in certain voluntary and direct grant institutions.

Home Office
The net increase of £92 million includes additions of £32 million for prisons and £19 million for police. There is also provision for additional expenditure by the Criminal Injuries Compensation Board and for a start-up loan to the Cable Authority, which is to supervise cable TV.

Defence
The provision allows for annual growth of some 3 per cent in real terms, with an addition for Falklands costs.

Social Security and Health
The programme provides for an uprating in November 1984 based on the rise in prices in the 12 months to May 1984, although the precise uprating for individual benefits will not be announced until June when the May index of retail prices (RPI) becomes available. Main policy changes are reductions in the coverage of help with housing costs, particularly housing benefits. The net effect is an increase on previous plans of £163 million.

Provision for the hospital and community health services should provide growth of nearly 1 per cent for the increasing number of very old people. Cost improvement programmes should release further resources to meet medical advances, reduce treatment shortages and waiting times, and allow other improvements. The provision for capital spending is being increased over this year's level by rather more than the forecast of general inflation. The provision planned for the family practitioner services allows for estimated demand. The provision for personal social services has been increased.

Local authorities
In the face of continued overspending the Government have been obliged to increase provision for current expenditure relevant for rate support grant (RSG) for 1984–85 by just under £600 million from the plans underlying the last PEWP. Provision will be £24.3 billion. This should enable the Government's policies for individual services to be broadly maintained.

Local authorities have been given provisional targets for total expenditure based on the revised provision for current expenditure.

Authorities which exceed their targets or guidelines will lose grant. (In 1983–84, some £292 million of grant has been 'held back' from authorities in England and Wales in the face of planned overspending; £45 million has been abated from grant in Scotland and four authorities have been required to make rate reductions equivalent to £19 million.)

Early returns from the local authorities for 1983–84 suggest no repetition of the massive capital underspending in 1981–82 and 1982–83. Overall, expenditure is expected to be within about £¼ billion of the planned level of just under £4 billion.

Environment – housing
It is proposed that local authority, housing corporation and other gross capital expenditure in the housing field should be set at £3,245 million, almost exactly the same in cash terms as this year's provision. The Secretary of State for the Environment has announced separately measures to ensure that better use is made of the available provision and particularly of the growing volume of capital receipts from the sale of council houses. These increased receipts, together with other changes, will produce a reduction in the net programme total of £497 million.

Table 10 Public expenditure plans

	1983–84	1984–85		£ million
	White paper (Cmnd 8789) with Budget and other pre-survey changes[1]	White paper (Cmnd 8789)	White paper (Cmnd 8789) with Budget and other pre-survey changes	Revised plans[2]
Departments (excluding nationalised industries' external finance)[3]				
Ministry of Defence	15 716	17 288	17 270	17 010
Foreign and Commonwealth Office (including Overseas Development Administration)	1 719	1 801	1 806	1 807
European Community	380	450	450	450
Intervention Board for Agricultural Produce	1 274	835	825	1 247
Agriculture	992	998	994	1 009
Forestry Commission	59	60	60	56
Department of Trade and Industry	1 488	1 370	1 411	1 351
Department of Energy	470	457	457	543
Export Credits Guarantee Department	55	164	164	166
Department of Employment	2 981	3 317	3 376	3 308
Department of Transport	3 366	3 466	3 546	3 537
DOE – Housing	2 709	2 988	2 993	2 496
DOE – Property Services Agency	−145	−115	−116	−92
DOE – Other Environmental Services	3 186	3 227	3 210	3 209
Home Office	4 041	4 253	4 241	4 333
Lord Chancellor's Department	449	509	509	501
Department of Education and Science	12 583	12 912	12 877	13 052
Office of Arts and Libraries	560	584	585	595
DHSS – Health and Personal Social Services	14 478	15 382	15 328	15 414
DHSS – Social Security	34 783	35 939	36 687	36 850
Civil Superannuation	937	1 017	1 036	1 053
Scotland[4]	6 160	6 339	6 339	6 318
Wales[4]	2 397	2 486	2 480	2 459
Northern Ireland	3 796	4 019	4 031	4 020
Other Departments	1 967	2 058	2 069	2 116
Adjustment for refund of VAT on certain services contracted out by Government departments	—	—	—	−30
Nationalised industries	2 748	2 615	2 548	1 882
Local authority current expenditure not allocated to departments	904	455	455	625
Special sales of assets	−1 250	−1 500	−1 500	−1 900
Reserve	1 040	3 000	3 000	3 000
PLANNING TOTAL	**119 843**	**126 374**	**127 131**	**126 385**

(1) Including measures announced on 7 July 1983 and changes of classification.
(2) Some figures may be subject to detailed technical amendment before publication of the 1984 PEWP.
(3) Provision for pay in these programmes reflects the pay factor of 3 per cent announced on 15 September 1983.
(4) Excluding agricultural expenditure, which is included in the agricultural line.

NATIONAL INSURANCE CONTRIBUTIONS

National insurance contribution rates for employers and employees are to remain unchanged but there will, as usual, be an adjustment in the earnings limit, and the Treasury supplement will be reduced.

Contributions are currently payable on all earnings, once the lower earnings limit of £32.50 a week is reached, up to the upper earnings limit of £235 a week. The lower earnings limit will now increase to £34 a week, in line with the single rate retirement pension, and the upper earnings limit to £250. There will be similar increases to the limit for self-employed contributions.

The current full rate of class one contributions will continue at 9 per cent for employees and 10.45 per cent for employers. The Treasury supplement, equal to 13 per cent of contributions (before taking account of the rebate for contracted-out contributions), will be reduced to 11 per cent.

ASSUMPTIONS USED BY GOVERNMENT ACTUARY

Each year the Government Actuary reports on what changes in contributions he thinks necessary to maintain the balance in the national insurance fund. Contributions are not a tax and are paid into the national insurance fund and the redundancy and maternity pay funds, as well as being used to help pay for the National Health Service.

The Government Actuary uses certain assumptions to assess what both the income of the national insurance fund and the payment from it are likely to be in the coming year. These working assumptions, which are not forecasts or predictions, are currently that:

(i) the number unemployed, excluding school-leavers, averages 2,850,000 in both 1983–84 and 1984–85 and that, in addition, the number of unemployed school-leavers and students or persons whose employment has temporarily stopped averages 180,000 in 1983–84 and 170,000 in 1984–85;
(ii) average earnings in the tax year 1983–84 are 7 per cent higher than in 1982–83 and the average in the tax year 1984–85 6½ per cent higher than in 1983–84. These are increases in average earnings over the economy as a whole and the latter figure takes account of the cash provision of 3 per cent made by the Government, in planning public expenditure for 1984–85, for average increases in wage and salary bills for the public services from due settlement dates;
(iii) the movement in prices between May 1983 and May 1984 (the relevant period for the November 1984 benefit uprating) will be 5½ per cent.

TAX READY RECKONERS

The tables below show illustrative changes to the major taxes and estimates of their direct revenue effects at forecast 1984–85 price and income levels.

The tables are published to inform discussion and help commentators and those making budget representations by providing 'building blocks'. Care should be exercised in fitting them together (pages 28–29 of the *Autumn Statement* give detailed guidance on use). It is, of course, not yet known what the increase in the index of retail prices will be between December 1982 and December 1983, the figure which governs statutory indexation. The figure of 5 per cent is an illustrative assumption.

First-year and full-year effects
The figures given are for full-year effects and also for the effect in the first year (1984–85); that is, the part of the full-year effect which would be expected to come through in tax receipts in that financial year. The two figures are different as some revenues affected by changes are received by the Exchequer after the end of the first financial year. Nor are the first-year revenue effects the same as the effects on the public sector borrowing requirement for that year. These differences occur because of the second-round effects of tax changes on the economy.

Basis of the calculations
Estimates of the size of the direct effects of tax changes depend on economic variables, such as prices, earnings, consumers' expenditure, etc., and so may alter as the prospects change. The illustrative tax changes shown are based on a view of the economy that is consistent with the prospects described in the *Autumn Statement*. There are in principle a number of ways of measuring the direct effect on revenue of a tax change, depending on whether assumptions are made about changes in the tax base and whether revenue from other taxes is included. The definitions used here are explained in more detail in *Economic Progress Report*, March 1981 (page 15), and in the 1981–82 *Financial Statement and Budget Report*.

Table 11 Income tax

	1983–84	1984–85
Allowances	£	£
Single and wife's earned income allowance	1 785	1 875
Married allowance	2 795	2 935
Additional personal and widow's bereavement allowance	1 010	1 060
Single age allowance	2 360	2 480
Married age allowance	3 755	3 945
Aged income limit	7 600	8 000

Income tax rates	Bands of taxable income	
	1983–84	1984–85
per cent	£	£
30	0–14 600	0–15 400
40	14 601–17 200	15 401–18 200
45	17 201–21 800	18 201–23 100
50	21 801–28 900	23 101–30 600
55	28 901–36 000	30 601–38 100
60	over 36 000	over 38 100

	1983–84	1984–85
	£	£
Investment income surcharge threshold	7 100	7 500

Table 12 Costs of indexation

£ million at forecast 1984–85 prices, incomes and capital values

	First year cost		Full year cost	
Indexation of income tax allowances and thresholds of which:	800		1 045	
Increases in main personal allowances		730		900
Increases in the basic rate limit[1]		40		70
Increases in further higher rate thresholds[1]		30		60
Increases in investment income surcharge threshold		Negligible		15
Indexation of capital transfer tax thresholds and bands	15		35	
Indexation of capital gains tax exempt amounts	Nil		10	

(1) Additional costs after previous changes have been introduced.

Indexation of direct taxes
If income tax allowances, thresholds and bands were adjusted to reflect indexation by an illustrative 5 per cent the 1984–85 levels would be as shown in table 11. The rules for rounding-up set out in the 1980 Finance Act (for income tax) have been followed. The figures for 1983–84 are shown for comparison. The costs of this indexation are given in table 12.

Table 13 Revenue effects of indirect tax changes

£ million 1984–85 prices and income levels

	Current level of duty on typical item[2]	5% Revalorisation[1]: Price change inc. VAT (pence)	Full year yield[3] £m	Unit changes from present levels of duty: Price change inc. VAT	Actual percentage change in duty %	Full year[3] yield/cost £m
Indirect taxes						
Beer (pint)	15·1p	0·9	80	1p	5·7	95
Wine (bottle of table wine 75 cl)	84·75p	4·9	25	1p	1·0	5
Spirits (bottle)	£4·56	26·2	25	1p	0·2	1
Tobacco (20 king size cigarettes)[4]	66·2p	3·3	110	1p	1·5	35
Petrol (gallon)	74·1p	4·3	210	1p	1·2	50
Derv (gallon)	62·83p	3·6	50	1p	1·4	12½
VED (cars and light vans)	£85	£4·25	77	£1	1·2	18
VED (goods vehicles)	£150–£2 940	£7·50–£147	19	£1·50–£29·40	1·0	3·8

(1) An 'across the board' revalorisation by 5 per cent (including the minor duties not shown above) would yield about £600 million in a full year, and the impact on the RPI would be to raise it by less than ¼ per cent.
(2) VAT is payable in addition to the duty except in the case of VED.
(3) Assuming for illustrative purposes implementation on 1 April, the first and full-year yield of changes in excise duties would be identical for petrol, derv and VED; for beer and tobacco the first-year yield would be approximately eleven-twelfths of the full-year yield; and for wine and spirits it would be approximately twenty-three twenty-fourths.
(4) The duty on cigarettes has *ad valorem* and specific elements; the percentage change relates only to the specific element, but the price change includes the subsequent increase in *ad valorem* duty and VAT.

Table 14 Direct effects of specimen changes in income tax and corporation tax

£ million at forecast 1984–85 income levels

	First year cost/yield	Full year cost/yield
Income tax[1]		
Rates		
Change basic rate by 1p[2]	950	1 025
Change all higher rates by 1p	35	70
Personal allowances		
Change single and wife's earned income allowance by £20	63	76
Change married allowance by £20	52	64
Change single age allowance by £20	5	7
Change married age allowance by £20	4	5
Change aged income limit by £100	2	3
Change all main personal allowances by 1%	145	177
Change (raise −/lower +) all main personal allowances by 10%	−1 415/+1 470	−1 735/+1 805
Higher rate bands		
Change (raise −/lower +) all higher rate thresholds by 1%	−12/+12	−21/+22
Change (raise −/lower +) all higher rate thresholds by 10%	−110/+140	−190/+245
Investment income surcharge		
Change (raise −/lower +) threshold by £500	−1/+1	−17/+19
Change rate by 1p	1	19
Allowances and thresholds		
Change all main personal allowances and higher rate and investment income surcharge thresholds by 1%	162	201
Change (raise −/lower +) all main personal allowances and higher rate and investment income surcharge thresholds by 10%	−1 575/+1 690	−1 945/+2 090

Corporation tax[3]

£ million

	First year	Full year
Change rate by 1 percentage point[4]	100	170
Change small companies' rate by 1 percentage point	10	18

(1) Changes are from the indexed levels of allowances and thresholds shown in table 11. Percentage changes are, however, of 1983–84 levels.
(2) Including the effect of the change on receipts of advance corporation tax and on consequent liability to mainstream corporation tax.
(3) Assessment to corporation tax normally relates to the preceding year. These are, therefore, the changes to revenue that would occur if the changed rates were applied to forecast 1983–84 income levels.
(4) Assuming small companies' rate unchanged.

Direct revenue effects

Table 14 gives estimates of the direct effects (at forecast levels of 1984–85 prices and incomes) of changes in the main personal allowances, thresholds and rates of income tax from the indexed level of allowances and thresholds set out in table 11. For corporation tax the table shows the effect of a 1 percentage point change in the rate of tax and in the small companies' rate. It shows the costs or yields resulting from individual allowances changes of £20 and of changes in all allowances by 1 and 10 per cent of their 1983–84 values. It also shows the effect of a package which changes all main personal allowances and higher-rate and investment income surcharge thresholds by 1 per cent and 10 per cent. These changes have been calculated as percentages of the 1983–84 levels and the effects estimated on top of the 5 per cent illustrative indexation.

Indirect taxes

Figures for changes in excise duties are shown in table 13. The first section shows the extra revenue from the individual duties if they were to be increased by exactly 5 per cent, together with the price increase that would result (after allowing for consequential VAT).

The second section shows for most duties the revenue yield from changing current level of duty so that (after VAT) the price of a typical item is changed by exactly one penny. For vehicle excise duty a £1 change for cars and light vans and a 1 per cent change for goods vehicles is shown.

Table 15 shows the revenue effects of 1 percentage point change in the rates of VAT and the national insurance surcharge.

Table 15 VAT and NIS

	First year[1] yield/cost	Full year yield/cost
1% point change in rate of VAT	550	740
1% point change in NIS assuming	1 180	1 330
recovery from the public sector	750	850

(1) Assuming implementation on 1 April.

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