



Treasury Chambers, Parliament Street, SW1P 3AG

Dear Andrew

Here is a final complete brief
on the PE White Paper.

Yours etc

JSL

SUMMARY BRIEF - KEY POINTS FOR THE PRESS CONFERENCE

TIMINGQ1. Why is the White Paper later than last year?

It is only a fortnight later - mainly because the General Election held up the timetable of the 1983 expenditure survey. It is still over a month earlier than in other recent years.

OUTTURN 1983-84Q2. What accounts for the increase from £119.8 billion in the Autumn Statement to £120.3 billion now?

The figure of £119.8 related to plans. Likely spending against the plans was allowed for in Table 1.7 of the Autumn Statement which forecast General Government Expenditure in 1983-84 of £120.5 billion. The White Paper's estimated outturn for the planning total of £120.3 billion is consistent with that earlier view.

Q3. Effect on PSBR?

Developments on public spending since the Autumn Statement do not conflict with our estimate of the PSBR at that time. But even at this stage of the year potential margin of error is considerable on any forecast of the PSBR. A later estimate will appear in the FSR on Budget day.

Q4. If there is overspending, why do you still show £300 million of shortfall?

The programme figures reflect spending departments' views of outturn. The £300 million is the Treasury's estimate of the net shortfall which is not reflected in departments' returns.

Q5. Was last year's White Paper estimate of shortfall then mistaken?

The 1982-83 outturn showed that departments were collectively spending much closer to their cash limits than we expected. The figure for the current year assumes that this will be repeated, though this is still uncertain (especially with the move to end-year flexibility) and we shall be watching the position closely in the coming weeks. There have also been some significant overruns on some demand-led programmes.

Q6. Significant breaches of cash limits in 1983-84?

The possibility of isolated breaches of individual cash limits cannot be excluded. A small number of cash limits are being adjusted in the context of Spring Supplementary Estimates. But in general Departments are expected to keep within their cash limits, including the reductions announced last July.

OVERSPENDING - GENERAL

Q7. There have been overspends in two of the last 3 years. Doesn't that invalidate your claim to be keeping to the plans? Are they unrealistically low?

The overspend in those two years was 0.3 per cent and 0.6 per cent. That is small in relation to the great uncertainties over demand-led expenditure and continued overspending by local authorities. The new-style reserve is intended to exercise a greater control over such increases in future. (Even in those two years the outturn was within the total of programmes plus the reserve. It was the allowance for shortfall which proved mistaken. The figures do not reveal a loss of control. They show relatively small errors in forecasting an item which has been particularly difficult to estimate.)

Q8. Why has gross debt interest gone up so much since the last White Paper?

A major factor has been higher than expected borrowing in 1982-83 and 1983-84. Other contributory factors were higher than expected interest payments by public corporations to the private sector and overseas, more up-to-date estimates of outturn and higher expenditure on interest support costs. The underlying interest rate assumptions have not been increased.

SHORTFALL IN 1984-85?

Q9. Why no shortfall shown for 1984-85?

Under the new arrangements for the reserve, all increases in programmes during the year must either be offset or charged to the reserve. So any overall underspending will eventually show up as an underspend of the new-style reserve. Whether that will happen in 1984-85 (and if so by how much) is a forecasting judgement which it was too early to make when the White Paper went to print.

[IF PRESSED FOR A FIGURE: Wait for the FSBR. Situation will be reviewed continually between now and the Budget.]

Q10. Did you consider the possibility of shortfall in setting the Reserve?

The possibility of shortfall in some areas is one of many judgements we made in setting the Reserve. We have always said there is no presumption that in any year the reserve will be fully spent.

"REAL TERMS" COMPARISONS

Q11. Has not the planning total for 1984-85 increased by over £1 billion in cost terms since the last Budget?

Yes. In cost terms there has been an increase of about 0.9 per cent. That does not result from any increase in the cash plans. It results entirely from

a fall in the expected rate of inflation. The fact that the money will now buy more is one of the benefits of reducing inflation; and one of the factors which has helped us to hold to the cash plans.

Q12. Why not recoup this £1 billion by reducing cash total?

Saw no reason to do so. Reasonable that public should derive some benefit from effect on services of lower inflation. Cannot fine-tune programmes to reflect every small variation in the forecast rate of inflation.

ASSUMPTIONS

Q13. Do the cash increases of 5 per cent, 4½ per cent and 3½ per cent represent your view of inflation in the next 3 years? Assumptions about pay in later years?

With the exception of social security and the pay factor announced for 1984-85, there are no explicit inflation assumptions underlying the plans; and the average cash increases in the planning total reflect other factors as well as prices - for example, changes in levels of service and improvements in efficiency. But the overall cash provision is generally consistent with the Government's intentions (i) to exercise a continuing downward pressure on inflation, and (ii) that in cost terms the pattern of expenditure over the period should remain broadly stable. Up-to-date assumptions about inflation for all three years will be published at Budget time in the FSR.

Q12. Why are you forecasting a steady level of 2.85 million unemployed?

We are not. The flat path shown for unemployment is a long-established convention; the actual level will depend on developments in the world economy and at home.

Q15. Isn't 3 per cent for increases in pay an unrealistic provision?

We believe that 3 per cent is a reasonable provision overall. But we are committed to genuine negotiations with the unions over the level of this year's pay settlement.

"HIDDEN MANIFESTO"/LONG TERM DEBATE

Q16. Does the White Paper tell the whole story? More cuts to come?

The White Paper shows quite clearly that there was and is no "hidden manifesto" of cuts and reductions in the public services.

Q17. Document on the long-term?

The Chancellor has made it clear that the Government wishes to make some more formal contribution to the public debate. He announced in the House on 9 February that he will publish a Green Paper "in due course".

[If pressed, precise timing not settled. Cannot anticipate content of Green Paper today.]

THE RESERVE

Q18. How does new-style reserve improve control?

Present practice where only discretionary increases in expenditure are charged to Reserve too limited. The bigger variations tend to arise from "estimating" changes, particularly on demand-led, non cash limited programmes. Under new arrangements, all increases which cannot be absorbed within programme totals will be charged to the Reserve. This will be much better geared to "control total" approach and to managing expenditure within the aggregate cash plans.

Q19. Will you identify the component elements of the new-style reserve?

New Reserve will be treated as a whole. Idea is definitely not to create two Reserves, one for discretionary and the other for estimating changes.

At any one time will obviously have a view about likely pressures on the Reserve from both discretionary and non-discretionary sources. But

position can change substantially. Judgement of scope for absorbing discretionary changes must take account of developments on demand-led programmes.

Q20. Why such big reserves for later years?

Reflects extended scope of reserve and future uncertainties. Figures will be reviewed in subsequent Surveys in light of experience of the new system in 1984-85.

CAPITAL EXPENDITURE

Q.21 In the new capital table aren't you just throwing everything in to boost the figures?

Not a fair or accurate suggestion. It has been widely stated that public sector capital spending has been falling. This table shows in a commonsense way what the public sector has spent on all capital goods and services in each year since 1978-79. Nothing illegitimate has been included. The level of capital spending in real terms has been virtually stable since 1978-79. The picture is much the same if you take capital spending as a share of GDP - 8.0 per cent a year to 1980-81 and 7.5 per cent since. The table shows the impact of new work generated by the public sector.

Q22. But the share of construction within the total has seriously declined?

There is no "right" level of such spending. It depends on whether the investment will earn a satisfactory return. If so, we are happy to encourage it. Remember too that Table 1.13 does not include work on repair and maintenance. This has steadily increased. In the early 1970s it was about 30 per cent of the total work supplied to the industry by the public sector. In 1982 it was about 50 per cent. So there is a lot of work not shown here which has been increasing.

Q23. Why include defence - surely not productive?

Defence capital expenditure provides work for the capital goods and construction industries so it should be included in the Table. There is no practical difference to the supplying industries between a civil and a military ship or aircraft, or between civil and military buildings. It all generates work of a capital nature. Spare parts, ammunition and so on have not been included.

Q24. But are we not running down the capital stock/failing to maintain the built infrastructure etc?

There are no very firm figures for public sector capital consumption. In any case there is no necessary presumption that it should be maintained intact at its past level. The essential thing is that proposals for replacement and improvements should earn an adequate return and be appropriate to the public sector.

Q25. Why not do more to encourage capital spending?

Not a question of "capital good current bad". Much current expenditure essential and some is an equally good investment in the future - training and R & D for example. But always happy to encourage capital projects which earn a satisfactory return.

Q26. You deduct asset sales from total spending but not from Table 1.13.

Why?

Just as the acquisition of an asset adds to total burden of public expenditure so the sale of an asset reduces it. We treat them symmetrically within the planning total which is an overall control total. Table 1.13 serves a quite different purpose. Receipts from the sale of

council houses etc self-evidently do not to reduce the public sector's capital purchases from the industries, so they are not deducted in Table 1.13.

DEFENCE

Q27. Have you abandoned the NATO commitment?

Provision up to 1985-86 fulfils the Government's commitment to meet the NATO aim of 3 per cent real growth per annum, with Falklands costs on top. The commitment has not been extended beyond 1985-86. The 1986-87 defence budget, Falklands costs exclusive, will be some £700m higher than the previous year. (The Falklands inclusive increase will be £600m. This is because additional Falklands costs in 1986-87 (£450m) are £100m lower than the 1985-86 figure.)

Q28. What is the total Falklands cost? Is it justified?

Provision over the period is about £3 billion including £780 million in 1982-83. Have no doubt that most people would accept it is fully justified so long as any threat to the Falklands can be foreseen.

EUROPE

Q29. Why is the net payments figure for 1984-85 £75 million lower than in the Autumn Statement?

The fall in 1984-85 reflects a number of factors. On the basis of the exchange rate assumptions used in constructing the projection, our VAT payments in 1984-85 are likely to be somewhat reduced. We are also assuming a larger refund in respect of 1984 than that agreed at the Stuttgart Council in respect of 1983.

Q30. The figures are on an upward trend. Is the Government concerned about this?

The projections are uncertain for the reasons given. The Government is concerned that our corrected net contribution to the Community Budget should be at a level which is fair. It has proposed that a "safety net" ought to be introduced, which would limit our corrected net contribution to our ability to pay, as measured by relative prosperity. This is currently the subject of negotiation within the Community.

AGRICULTURE/IBAP

Q31. Why such large increases for IBAP?

This represents expenditure by IBAP on agricultural support under the CAP. About one-third of the increase is for expenditure which is pre-funded from the Community Budget. The rest reflects forecast extra intervention purchases, particularly for milk products: these costs fall initially on the Exchequer, but they are recouped from sales and by Community reimbursement for losses when intervention stocks are sold.

HOUSING

Q32. How do you justify such a large further cut in housing?

The Housing figures in Part 1 of the White Paper are shown net of receipts. Most of the apparent cut in 1984-85 results from an increase in receipts of about £300 million. The gross provision for capital expenditure in 1984-85 - which is what matters to the general public and the industry - is about the same as for 1983-84.

Q33. Why end temporary Home Improvement Grants?

These measures, introduced in the 1982 Budget, were clearly stated to be temporary. They were designed to take up immediate capacity in the building industry. The original deadline for applications was twice extended and has now been confirmed as 31 March 1984.

HEALTH

Q34. Do the plans meet your election pledges?

They more than do so. The new plans are for spending £845m more in 1984-85 than in 1983-84, and for £877m more in 1985-86 than in 1984-85. The Prime Minister's Edinburgh speech promised increases of £800m and £700m respectively.

Q35. Higher prescription charges?

The Social Services Secretary will be announcing changes later, but the exemptions from charges will remain.

SOCIAL SECURITY

Q36. Is social security expenditure out of control?

No. The reasons for the increases are given in paragraph 8 of Part 1. About half the increase is accounted for by specific policy decisions. The rest is accounted for by estimating changes. We are, however, reviewing procedures for forecasting these demand-led expenditures which are particularly difficult to estimate.

Q37. Why the increase of £360m for 1984-85 since the Autumn Statement?

In the White Paper we have been able to take account of more up-to-date estimates of expenditure on benefits, mainly supplementary benefits.

Q38. Are there more announcements of cuts to come?

There are no plans for further reductions in the programme total. There may be more or less spent on individual benefits as normal part of policy review. Mr Fowler will announce details of November uprating in June.

[If pressed: Mr Fowler is to find some offsetting savings for concessions on housing benefit; this will involve some adjustments within programme total, as well as small (£8m) addition to programme from contingency reserve.]

Q39. Why did you cut housing benefit?

Some savings in the overall social security budget are essential if the increasing cost to the taxpayer is to be kept within reasonable limits. Housing benefit now goes to 1 in 3 households, 40 per cent of the population. Some of these have above average earnings. Cuts affect households best able to afford them. Most pensioner claimants will not be affected. No one on supplementary benefit need be affected.

Q40. But haven't you had to climb down on this?

The modifications announced on 6 February will ease the particular problems identified by the Social Services Advisory Committee. They will give families affected longer to adjust and help local authorities with the administrative task of making the changes. The modifications will not add to the existing expenditure plans.

Q41. Will housing benefit changes deepen or widen the poverty trap?

The trap will be less wide - ie there will be fewer people in it (those who lose benefit will come out). It will be deeper, ie marginal rates will be higher. But the changes mainly affect people above the worst part of the poverty trap.

LOCAL AUTHORITIES

Q42. Is not provision for LA current wholly unrealistic?

No. The targets set allow authorities which have kept spending down a 3 per cent increase over budgets. Authorities which have failed to meet previous targets are faced with a maximum 6 per cent cash cut. Up to authorities now to control their own costs.

Q43. Means high rate rises?

Not if authorities budget sensibly.

Q44. Now penalising responsible authorities?

No authority meeting its targets will lose grant through hold-back. All depends on local authority decisions.

Q45. What saving have you assumed from rate-capping?

The scheme will operate for the first time in 1985-86. The first 12-20 authorities will be selected once Parliament enacts the Bill. There will then be expenditure savings and it will be possible for the target and penalty system to be fairer on authorities who have kept spending down.

Q46. What about LA capital? Still underspending?

Provision for LA capital (almost £3.7 billion) is about the same as forecast outturn for 1983-84. Past high level of underspending seems unlikely to be repeated this year. Likely to be within £250 million of levels given in last White Paper (£3.9 billion).

ASSET SALES

Q47. Latest position on British Telecom and British Airways?

Nothing to add to stated position that sale of BT is planned for next autumn with BA in early 1985.

Q48. What do future year targets imply for method of BT sale?

No final decision has yet been taken on the method of BT sale. Always some uncertainty about level of receipts, but level of £1.9 billion in 1984-85 and £2 billion in each of next 2 years is a realistic and achievable target.

Q49. Future plans?

Not the practice to reveal composition of future sales programmes. Determined by market and commercial considerations and commonsense.

Q50. Frittering away the nation's assets on current spending?

No. It is entirely reasonable to dispose of unwanted assets, particularly where this will increase competition in the economy and help to promote greater efficiency. Treatment of special sales is fully consistent with sales of land, council houses and other assets which also reduce public expenditure.

NATIONALISED INDUSTRIES

Q51. Are you tightening the screw on the industries/forcing them to put up prices?

The fall in their need for external finance arises mainly from further improvements in costs and performance. For 1984-85, industry tariffs are expected to rise at or slightly below the rate of increase in the RPI.

Q52. What about industries' investment?

Allowing for privatisation, investment in 1983-84 is expected to be 12 per cent up on 1982-83 and to be much closer to plan than in previous years. (The apparent fall between 1983-84 and 1984-85 and later reflects the privatisation of British Telecom, BA and Enterprise Oil, whose investment will then be in the private sector.)

Q53. Electricity prices?

The Government suggested a 2 per cent increase in April to give confidence that the electricity supply industry would meet its EFL (-£740 million) and to avoid the risk of sudden large increases later. This rise is consistent with economic pricing and is lower than expected when the present financial target was set a year ago.

BRIEFING FOR THE 1984 PUBLIC EXPENDITURE WHITE PAPERA: GEP briefs

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FACT SHEET - KEY COMPARISONS

Public expenditure held within previous plans:

	Cmnd 8789	Autumn Statement	£ billion Cmnd 9143
1984-85	126.4	126.4	126.4
1985-86	132.3	-	132.1

Fall in ratio to GDP

1983-84 Plan	Outturn	1984-85 Plan
43½%	43%	42%

Rise in cost terms
comparing plan with
plan. NB Not
comparing plan with
outturn

1983-84 Plan	Estimated Outturn	£ billion 1984-85 Plan
113.9 (Cmnd 8789)	114.6 (Cmnd 9153)	114.6 (Cmnd 9143)

Fall in rate
of increase
of public
expenditure

1978-79 on 1977-78 (last full Labour year)	1982-83 on 1981-82	1983-84 on 1982-83	1984-85 on 1983-84	1985-86 on 1984-85	1986-87 on 1985-86
+15.8%	+8.3%	+6.1%	+5.0%	+4.5%	+3.5%

1984-85 £ million

Main changes between
Cmnd 8789 and
Cmnd 9143

Agricultural support	+395
Local authority current expenditure	+600
Social Security	+1,268
Defence	-257
Housing	-492
Nat Ind EFL's	-700

Capital	1983-84 estimated outturn	1984-85 plan	%increase
Capital spending (new definition)	23.4	23.9	2% or £500m
Capital spending on new construction (Old definition)	10.9	10.9	0

Civil Service Manpower (see brief A10)

<u>Date</u>	<u>Number</u>	<u>% reduction</u>
1.4.79	732,300	-
1.4.82	666,400	9%
1.4.83	648,912	11%
1.1.84	632,600	13.6%
1.4.84	630,000(estimated)	14%
1.4.85	608,208 (estimate)	17%
1.4.88	593,000*(estimate)	19%

*6% reduction over 1.4.84 figure of 630.000

IMPROVEMENTS IN PRESENTATION

1. Volume 1

Volume 1 contains a new presentation of capital spending (Table 1.13) which gives a more complete picture of Government spending on capital goods. And manpower figures for Government departments are included for the first time (Table 1.15)

2. Volume 2: Clearer statement of objectives

Volume 2 of the Public Expenditure White Paper now contains clearer statements of the the policy objectives to which expenditure is directed; these will in turn be related to progress and performance indicators wherever possible. There are now some 550 output measures, an increase of 40 per cent since last year. All programmes now include some output measures.

3. References included for Estimates and Votes

The programme chapters on planned expenditure include references to the Estimates presented to Parliament for control purposes. The intention is that both the White Paper and the Estimates should, as far as possible be derived directly from the information systems which departments are already developing for the management of both programmes and their own activities and costs.

4. New contents pages for the text tables

A new item this year. A useful reference for locating text tables because of increased size of publication.

5. The change to the cover of the PEWP

This follows the layout approved by the Chancellor for the "family" of Treasury publications (Autumn Statement, FSBR and PEWP)

6. Part Four

Two new Tables 4.6 and 4.7. Procedure Committee's recommendations, to show more detail on how the public corporations are financed.

7. Part 3

Now includes all the Nationalised Industries text in one place. Water authorities included for the first time as separate item in part 3.

8. Volume 2 longer

Volume 2 this year is 172 pages compared with 130 pages last year. Length does not equal quality, but the increase reflects the improvements described above.

9. Analyses by Economic Category and Spending Authority.

The analyses of total public expenditure by economic category, and by spending authority and economic category are now carried through for the last two years of the survey. The figures for the last two years are very provisional.

1983-84 OUTTURN

1. Comparison with Autumn Statement?

The Autumn Statement planning total of £119.8 billion shown in Table 2.1 relates to plans, not estimated outturn. Consideration of the likely spending against those plans was allowed for in Table 1.7 and it should be evident that the White Paper estimated outturn of £120.3 billion does not represent a change in view since then.

2. PSBR overshooting?

The Autumn Statement increased the 1983-84 PSBR estimate in the Budget from £8.2 billion to £10 billion. This estimate incorporated the view of likely spending against the Autumn Statement plans and developments since then, on public expenditure, do not conflict with it. Even at this stage of the year the potential margin of error on any forecast of the PSBR is considerable. A later estimate will appear in the FSBR on Budget day.

3. Where has the overspending occurred?

Compared with Autumn Statement plans the White Paper estimated outturn, after broadly assessing where the £300 million shortfall is likely to occur, consists of £½ billion overspend on central government expenditure and £1½ billion on local authority current expenditure partially offset by nearly £½ billion underspend on nationalised industries EFLs and an unspent Contingency Reserve of around £½ billion. The total net overspend, £½ billion, is unchanged from the view taken at the time of the Autumn Statement although some of the components have change very slightly.

4. If there is overspending why does shortfall appear in the White Paper?

The overspending is against Autumn Statement plans, the shortfall is against departmental views of outturn. The £300 million shortfall is the Treasury's estimate of the net shortfall which is not reflected in departmental returns.

5. Why is the 1982-83 outturn in Financial Statistics Table 2.4 so different from that in the White Paper? And 1981-82?

The figures derived from national accounts sources in Table 2.4 allow for known differences between general government expenditure, as measured in the national accounts, and the planning total. The reconciliation between these figures and the White Paper figures is a continuous process and more work needs to be done. Unexplained differences, though unsatisfactorily high, are low in relation to planning total as a whole.

CHANGES SINCE CMND 8789

There have been few changes to the plans for 1984-85 since Cmnd 8789. The net result has been a £35m fall in the planning total. Table 4.2 provides details of the changes.

2. Agricultural support expenditure has risen £395 million since Cmnd 8789 due to increases in Intervention Board for Agricultural Produce spending, particularly on milk products.

3. Local authority current expenditure is £600 million higher than planned.

4. Social Security expenditure increased £1300 million since Cmnd 8789. Reasons include increases in child benefits and one parent benefit and effects of changes in uprating assumptions. Plans for next year show a rise of £360 million since Autumn Statement mainly because of revised estimates of expenditure on supplementary benefits.

5. Housing provision is £600 million lower than in Cmnd 8789 due to higher receipts and lower current expenditure.

6. Defence expenditure is £257 million lower than in Cmnd 8789. The effects of the March 1983 NIS reduction, and the 1983-84 cash limit cut were reflected in the autumn statement figures. The defence budget is now £21 million higher principally due to the transfer of COI services to repayment basis and an adjustment to the charging basis for fishing protection.

7. The Central Office of Inflation^{promotion} has now been put on a repayment basis. The PES provision has been transferred from Common Services to other programmes.

REAL TERMS COMPARISONS

1. Definition of cost terms

Cost terms figures are the cost figures adjusted for general inflation, as measured by the GDP deflator at market prices, to the base year 1982-83. The GDP deflators used for 1983-84 and 1984-85 are 5 per cent, as given in the Autumn Statement (paragraph 1.48). The cost terms figures for 1984-85 are not themselves plans - they are derived from the cash plans.

2. Why no cost terms figures beyond 1984-1985

The cost terms figures in Table 1.4 go only as far as 1984-85 because figures for the GDP deflators are not available for later years.

3. [NOT FOR USE]

(Last year a revised and extended cost terms table was published, by means of an arranged PQ, after the Budget. It took account of the GDP deflators given in the FSBR and of the effects of Budget changes on the public expenditure planning total in 1982-83 and 1983-84). If GDP deflators are given in the FSBR on Budget day we will suggest a similar procedure this year.

4. What the figures show: 1984-85

On the assumption of an increase in the general price level (as measured by the GDP deflator) of 5 per cent between 1983-84 and 1984-85, Table 1.14 shows that public expenditure expressed in cost terms is expected to be broadly stable between the two years.

5. Comparison with the cost terms figures in Table 2.2 of the Autumn Statement

For 1984-85, the PEWP cost terms figure is the same in rounded terms as in the Autumn Statement figure - this results entirely from the increase in the corresponding cash figures.

6. Comparison with 1983 Budget

The 1984-85 planning total expressed in cost terms in Table 1.14 is some £1.1 billion more

than the corresponding 1984-85 figure given in the past 1983 Budget cost terms PQ (Hansard 17 March WA Col 240) converted to base year 1982-83. This is because there has been a reduction in the expected rate of inflation, as measured by the GDP deflator in both 1983-84 and 1984-85, since the 1983 Budget. This does not mean that the expenditure plans for 1983-84 have increased. In fact the cash planning total for 1984-85 in the 1984 PEWP is virtually the same as in the 1983 PEWP. The fact that this planning total will now buy more in one of the benefits of reducing inflation. [The figures underlying the above are set out below:

	<u>1983 Budget</u>	<u>1984 White Paper</u>
Planning total, cash	126370	126353
	(1983 PEWP figure)	
Deflators, per cent		
1983-84	5.5	5.0
1984-85	5.5	5.0
Planning total, cost terms		
base year 1982-83	113540	114606

7. Should not all programmes have been revised downwards for 1984-85 as a result of falling inflation?

One of the main aims of cash planning is to require programme managers to plan to achieve optimum service levels within the cash constraints. Price changes, in general, have to be absorbed. Automatic downward adjustment to programmes when inflation falls would inevitably mean automatic upward adjustment if inflation was to rise. This would destroy the object of cash planning. The fact that the planning total for 1984-85 will now buy more is one of the benefits of reducing inflation.

ECONOMIC ASSUMPTIONS

Prices and Unemployment

1. Where are the economic assumptions published?

Economic assumptions on prices and unemployment are published in Part 1 paragraphs 7 and 42 and Part 2.12 paragraph 35. They are needed mainly for costing the social security programme. GDP deflators for 1985-86 and 1986-87 are not included but may be published in the FSBR on Budget day.

2. What are the figures

To calculate the social security programme, it is assumed that unemployment (GB narrow) will be 2.85 million in 1983-84 and subsequent years and that prices will rise by 5½ per cent in the twelve months to May 1984 and by 4½ per cent and 4 per cent respectively in the two subsequent years.

3. Any changes since Autumn Statement?

The assumptions for next year (1984-85) are the same as those already published in the Autumn Statement (paragraph 3.04) and by the Government Actuary in his latest report (Cmnd 9092). The PEWP extends the assumptions to the following two years when they become increasingly provisional.

4. Flat path for unemployment conventional?

The flat path for unemployment for the later years follows the usual convention; the actual level will depend on developments in the world economy and at home.

5. How have the assumptions changed since the last White Paper?

Unemployment is now projected as a flat 2.85 million instead of 3.02 million, mainly reflecting the effect of changes in the 1983 Budget which removed about 0.15 million people from the unemployment count. In comparing the price assumptions must bear in mind that those in Cmnd 8789 were for annual increases to November each year while the latest assumptions are May on May, following the return to the historical method of uprating social security benefits. The assumed uprating are in fact ½ per cent higher than Cmnd 8789 for both 1984 and 1985, but it is not surprising that May on May rises are slightly higher than November on November in view of continued downward trend in inflation. The underlying

price assumptions have hardly changed. The slight rise assumed in the first half of 1984 (reflected in the 5½ per cent figure for May 1984) should be seen as a temporary rise in an otherwise declining trend.

Interest rates

6. Working assumptions (not forecasts) on interest rates are used for costing some programmes eg export and shipbuilding credits and housing subsidies and, outside the planning total, debt interest - see note B12. It is not appropriate to publish the interest rate assumptions as they are market sensitive.

THE RESERVEPOSITIVE1. Reason for Change

Aim already established of operating the public expenditure planning total as a control total. Present practice where only expenditure increases for "decisions" are charged to the Reserve does not serve that purpose well. The bigger variations within planning total tend to arise from "estimating" changes, particularly on demand-led, non cash. limited programmes. New arrangements whereby all increases (which cannot be absorbed within programme totals) are charged will be much better geared to "control total" approach and to managing expenditure within the aggregate cash plans.

2. Change of Name

Will in future be simply termed "the Reserve" rather than "Contingency Reserve" to underline that all changes, not just one category, fall within its scope.

DEFENSIVE3. TCSC Recommendation:One or Two Reserves/Publish Component Parts/Reduction of Parliamentary Control

New Reserve will be treated as a unified whole. Idea is definitely not to create two Reserves, one for contingencies and the other for estimating changes. At any one time will obviously have a view about likely pressures on the Reserve from both discretionary and non discretionary sources. But position can change substantially. Whole purpose of new arrangement is to ensure management of Reserve can take account of these changes eg so that scope for absorbing discretionary increases takes account of developments on demand led expenditure and anticipated shortfall. Mistake to publish forecasts of how Reserve is expected to be spend when its role is as a control mechanism for keeping within planning total.

No question of reducing Parliamentary control. Reserve is an operational tool for Governments use in expenditure monitoring and control. Parliament will continue to have opportunity to scrutinise revisions to Departmental Estimates, both discretionary and non-discretionary as year proceeds.

4. Publication of State of the Reserve/Forecasts of Planning Total Outturn

No rigid plans about publication of details or latest forecasts as year progresses. [If necessary] Will obviously respond to questions about latest state of Reserve as year proceeds. [If pressed on provision for discretionary increases]. There is no precise allowance. But note that under old arrangements actual charges on the Reserve have been well below the Reserve total - £1145m out of £2500 m in 1981-82, £1400m out of £2400 m in 1982-83 and £750m-now estimated out of £1500m for 1983-84

5. Will Estimating Savings/Shortfall be added to Reserve?

Concept of Reserve as link between individual programme totals and aggregate planning total means that monitoring of the Reserve must take account of estimating reductions as well as estimating increases. In future shortfall will form one element of a net Reserve allowance. [If pressed . Shortfall has been taken into account in setting Reserve figure for 1984-85. No intention to withhold information provided in the past. Will consider publishing latest estimate of the shortfall component in the FSB].

6. Is aim now fully to spend the Reserve?

Never has been an object to spend all the Reserve, and the new arrangements make no difference to that. Size of 1984-85 Reserve has been fixed at a level which is thought adequate to ensure planning total is not over-run. Attitude to calls on it will obviously be influenced by the balance remaining, but won't be consciously trying to "spend out".

7. Will there be automatic access to Reserve for estimating increases?

Consideration will obviously be given to whether it is feasible or sensible to seek to absorb estimating increases elsewhere in programmes.

8. New arrangements unworkable Attempt to operate similar system in 1977 broke down.

Accurately monitoring and controlling aggregate spending of £126 billion has never been easy. New Reserve arrangements not a panacea, but a step in the right direction.

Continuing to make improvements in monitoring procedures. 1977 experience not a good precedent - we had "funny money" then coupled with a high and volatile rate of inflation. Now we have a much lower rate of inflation and a more stable economic conditions; and are firmly and successfully launched on cash planning.

9. What happens when Reserve is bust?

Hypothetical question; new system is intended to prevent that happening.

10. Big Reserve figures for later years

Figures will be reviewed in subsequent Surveys, in light of experience in 1984-85 with the new system.

CAPITAL EXPENDITURE

1. Why change the definition of capital expenditure?

The traditional definition of capital expenditure does not give good indication of the work supplied to the construction and capital goods industries. There are three problems with the traditional definition. First, it excludes the capital expenditure of the nationalised industries (it only includes their external finance). Second, it is measured net of asset sales such as council houses. Third, by international national accounting conventions, nearly all defence expenditure, much of which is of a capital nature, is classified as current expenditure.

2. Why include defence - it is not productive investment?

Defence capital expenditure provides work for the capital goods and construction industries so it should be included in this wider definition. For example, there is no difference between capital expenditure on a military hospital and that on a civilian hospital.

3. What is included/excluded from the NATO definition of defence capital expenditure?

The NATO definition includes expenditure on items of a capital nature as opposed to those you would associate with operating costs. Thus it includes expenditure on major equipment (missile systems, aircraft, ships etc) and construction on military buildings. It do not include repair and maintenance work, provision of spare parts or ammunition.

4. Why deduct asset sales from the planning total and add them back in the new table?

It would be wrong not to deduct asset sales in the planning total. This is a measure of public expenditure and as such should include the purchase of assets. They should therefore be deducted when they are sold. (This general principle is followed in both public expenditure and national accounts.) The new table is designed for a different purpose - it shows public spending on new assets. It excludes (where possible) the transfer of existing assets and estimates the value of public sector purchases of new capital goods and services.

5. Do these figures allow for capital consumption (ie depreciation) and if not what is net capital expenditure?

Capital expenditure in the White Paper does not make any allowance for capital

consumption. But data published in the national accounts does provide figures of net capital formation (ie gross domestic fixed capital formation less capital consumption) although the method of computing the capital consumption figures is necessarily fairly approximate. Table 11.4 in 1983 edition of National Income and Expenditure blue book shows net capital formation is continuing to be positive overall. But it has been running at a lower level in recent years and certain sectors (notably the manufacturing sector) are negative.

6. Trends in capital expenditure

Under the new definition, capital expenditure has been increasing in cash terms each year and in real terms has remained broadly stable since 1978-79 (see Table 1.13)

7. Table 1.9 shows capital expenditure planned to fall in cash terms through to 1986-87. Using GDP deflators in para 42 for 84-85, and price assumptions in para 35 of social security chapter for later years the fall in cost terms is much greater [28 per cent 1983-84 to 1986-87] Why?

Fall in lending to nationalised industries part of the explanation. Capital expenditure is not in itself a good thing. Each capital project has to be assessed on its merits. Plans for future are necessarily subject to revision in this field. The lower inflation and the lower current expenditure the more room will there be for public capital expenditure. No point increasing total public expenditure if that is just going to stop private sector capital investment by raising interest rates. New presentation of capital only goes up to 1984-85 because of uncertainty in this area. This follows the practice in previous PEWP's.

8. What is happening to capital expenditure on construction work?

Table 4.5 shows the figures for capital expenditure on construction work. In cash terms expenditure has increased between 1978-79 and 1983-84 but is expected to show a slight fall in 1984-85. However, although capital expenditure on construction work has been declining in real terms, more work on repair and maintenance is now being undertaken. This has steadily increased from about 30 per cent at the beginning of the 1970s to about 50 per cent in 1982 of the total work supplied by the public sector to the construction industry.

9. Capital/Current split

After adjustment for defence expenditure, the split between capital and current expenditure of general government (central and local) on goods and services has remained broadly stable since 1978-79. (Current expenditure on goods and services excludes social security which is included as current grants to the private sector). But some types of current expenditure are just as important in terms of investment as capital expenditure. For example, Research and Development, expenditure on industrial training etc. Also it can provide work for the private sector. For example, training and

for the construction industry, NHS purchasing drugs from the pharmaceutical industry.

10. Isn't proportion of capital still falling on the new definition?

Estimates on the new presentation of the capital proportion of total goods and services expenditure by central and local government show very little change in recent years. Even when current transfers, like fast growing social security, are included in the figures, the implied fall in capital share is small - 11½ per cent in 1978-79 to 11 per cent in 1984-85. Very difficult to do comparable current figures for nationalised industries.

11. Do the 1983-84 and 1984-85 figures of capital expenditure include an estimate for shortfall?

The planning total for 1983-84 assumes an overall level of shortfall of £300 million. It is not possible to break down this overall estimate with any precision. [NOT FOR USE: It is likely that the shortfall on the new definition of capital will be higher than this, probably about £600 million, about half of this will be by the nationalised industries, a quarter on defence (end-year flexibility will mean that it is moved into 1984-85) and the remainder by central and local government]. The 1984-85 figure is planned expenditure and does not include any allowance for shortfall.

12. Why have you dropped the old construction table?

The new definition is a more appropriate measure of public sector spending on capital goods and the work provided for the construction industry. But we have not dropped the construction table; it appears as Table 4.5 in Volume 2.

13. Why is the new definition of capital expenditure not used elsewhere in the White Paper?

The Table is designed to show the impact of capital expenditure on the capital goods and construction industries. Reasons for not adopting the three adjustments elsewhere are as follows:-

- a. nationalised industries are controlled through their external finance not their expenditure, so the planning total reflects this;

- b. standard convention in public expenditure and national accounts is to measure expenditure net of asset sales such as council houses;
- c. public expenditure follows national accounts convention on defence expenditure. We would not want public expenditure to move out of line with the national accounts.

RECENT DEVELOPMENTS IN THE UK ECONOMY

FACTUALFinancial Conditions

In last six months annualised rate growth in monetary aggregates around middle of 7-11 percent target range. PSBR between April and December 1983 estimated just over £10 billion (not out of line with forecast in Autumn Statement of £10 billion for financial year 1983-84 as usually substantial tax receipts in final January-March quarter). Three month and long term interest rates remained fairly stable in January. The dollar reached all-time high against sterling of around \$1.39 in early January but sterling relatively stable in "effective" terms against all currencies in the range 82 to 82½.

Inflation and Costs

(i) Domestic and external inflationary pressures remain subdued. In 1983 as a whole retail prices 4½ percent higher than 1982, lowest increase since 1967. Import prices remained steady since early 1983. Producer output price inflation (year on year) remained steady at 5½ percent during 1983H2, whilst producer input price inflation fluctuated between low of 6½ percent (July) and high of 9½ percent (September).

(ii) Year on year increase in whole economy average earnings remained at 7½ percent in recent months. Wage settlements (mfg) were about 5½ percent in 1983H2, according to CBI Pay Databank (compared with 6½ percent in the same period in 1982.) Unit wage costs rose at historically low rates in 1983.

(iii) Cost competitiveness in manufacturing (as measured by relative unit labour costs) estimated to have improved by around 20 percent since early 1981. Over same period UK unit labour costs have risen less than average of major competitors.

Company Sector Finances

Substantial improvement in financial situation of company sector. Total gross trading profits of non-North Sea industrial and commercial companies (net of stock appreciation) rose by 30 percent between 1982Q3 and 1983Q3. Real profits of these companies increased by about a third between 1981H1 and 1983H1, according to Bank of England. ICC's in financial surplus of £6½ million in first three quarters of 1983; as percentage of total final expenditure in economy this is highest since early 1970s. Liquidity now approaching 1978 peaks, according to latest DOI Survey of Company Liquidity. CBI forecast 7½ percent net real rate of return for 1984, compared with low of 4½ percent for 1982.

Output and Demand

(i) GDP (average) in 1983Q3 about 3 percent higher than year earlier; running above 1979 level.

(ii) Output of production industries continues to show steady growth and was 4 percent higher in 1983Q4 than year earlier and 7½ percent higher than its trough in 1981Q1.

(iii) Service industry output - over half of whole economy output - grown steadily to 1983Q3 and now about 2½ percent above 1979 average.

(iv) Manufacturing output (about quarter of whole economy output) recovered during 1983. Electrical engineering and chemicals have grown by 15 percent and 9 per cent respectively since 1981 trough.

(v) Consumers' expenditure and retail sales in 1983 3½ per cent and 5½ per cent respectively up on 1982. Total fixed investment in first three quarters of 1983 about 10 percent higher than first half of 1981.

External demand and the current account

Export volumes fluctuated considerably during 1983, increasing by 1½ percent between 1982 and 1983 as a whole, but increasing by 10 per cent in fourth quarter. Import volumes grew steadily during 1983 (reflecting continued strength of domestic demand) and were 7 percent higher in year as a whole compared to 1982. Current account-estimated £2 billion surplus in 1983 (cf. £5½ billion 1982) including £½ billion surplus in December. Deficit of almost £1 billion on visible trade more than offset by £3 billion surplus on invisibles.

Labour market

(i) Continued strengthening in demand for labour. Employed labour force increased by 87,000 1983Q1 to 1983Q3; about 200,000 new jobs in service sector in first three quarters of 1983. Short time working (mfg) at lowest level for four years, overtime working picked up strongly since last Summer. Vacancies up 59,000 since 1981 trough but have fallen in each of last 3 months.

(ii) There has been broad levelling out of seasonally adjusted adult unemployment (despite 29,000 recorded increase in January). Over last 6 months increase averaged 4,000 a month, cf. 21,000 a month over previous 6 months.

Forecasts

Industry Act forecast in Autumn Statement expects GDP growth of about 3 percent in 1984 with retail price inflation falling to 4½ percent by 1984 Q4. Consensus of outside forecasts for 1984 expects some small increases in year on year GDP growth, retail price inflation, and unemployment.

POSITIVE

1. Evidence for continued growth in activity?

Recovery becoming more broadly based - confirmed by CBI's Industrial Trends Survey (January), which shows growth spreading to capital goods producers and points to 7 per cent increase in manufacturing investment this year. Export volumes increased by about 10 per cent in 1983 Q4. Outside forecasters - including OECD - generally agree strong growth in investment and exports in prospect. This should complement continued strength in consumer demand.

2. Evidence of improvement in labour market?

The labour market continues to respond to rise in output. Total number of people at work - including self employed - now rising. Short-time working at lowest level for four years. Strong rise in overtime working since mid-1983. Vacancies up substantially since 1981.

DEFENSIVE

1. Recovery will falter this year because too narrowly based?

DTI Investment Intentions Survey further points to investment increasing 9 percent in manufacturing and 6 percent in services. Export volumes increased by about 10 percent in 1983 Q4. Outside forecasters - including OECD - generally agree strong growth in investment and exports in prospect. This should complement continued strength in consumer demand. Latest Trends Survey from CBI (Jan) presents evidence that recovery in mfg expected to become more broadly based. Nothing in recent movements of CSO's leading indicators to suggest activity will peak in the course of 1984.

2. January rise in adult unemployment means Chancellor's hopes for fall in 1984 look over-optimistic?

Wrong to place too much emphasis on one month's figures. After series of small monthly rises and falls January's figure appears to be an erratic movement. No grounds for changing assessment that there has been broad levelling out in seasonally adjusted unemployment. Over last 6 months increase has averaged 4,000 a month, compared with 21,000 a month over previous 6 months.

MANPOWERCIVIL SERVICEPOSITIVE1. Civil Service still too big/does too much/is over staffed?

Already there are 99,700 fewer staff in post than in April 1979. These results were achieved by reductions in functions, privatisation and improvements in efficiency. We are now confident of achieving the 630,000 target by April 1984. A further run-down to 593,000 by 1988 is planned.

DEFENSIVE2. Why do the Government's manpower plans after 1984 envisage only a relatively modest manpower reduction by 1988?

Given the very substantial reductions between 1980 and 1984 (14 per cent), it was not to be expected that there would be a reduction of similar size in the next four years. The planned reduction of 6 per cent between 1984 and 1988 is a net figure. The net reduction of just over 37,000 reflects gross reductions of some 60,000 offset by increases of around 23,000 eg some 5,400 for the prison service.

3. The Manpower cuts and departmental targets are arbitrary, and are damaging the quality of service?

They are not arbitrary. They are a considered judgement of what is necessary. Following rigorous departmental reviews the aim has been to match staff numbers as closely as possible to the essential work each department has to carry out. Sensible reductions were planned to take account of increased efficiency and transferring work out. But increases have been allowed where the needs of the work dictate, and a contingency margin included for unforeseen circumstances, eg changes in demand-led services. Great savings have been made with little adverse affect on provision of services.

4. Is the Government planning large reductions in public service manpower given that IMF study shows we have for too much?

The IMF study is misleading and inaccurate. Excluding the NHS, UK has much

the same number of public servants as the IMF would expect. IMF accept errors and are reprinting the document

5. Is the 1988 target the end of the Government's plans to reduce the Civil Service?

No. The Government intend to maintain a continuing downward pressure on the size of the Civil Service. Departmental manpower figures will be reviewed each year in the Public Expenditure Survey. The presumption is that the figures will be adhered to, or reduced further where possible.

6. Why reduce numbers of staff who gather in money (Customs, Inland Revenue)?

We have to balance all the factors. Preventing under-payment of tax or over-payment of benefits is important. And so is the level of public spending. Adjustments can be made, within manpower limits, to meet particular requirements. In the Revenue Departments the number of specialist investigatory staff is greater than before the last Parliament (75 per cent in Inland Revenue and 30 per cent in Customs).

ARMED FORCES

DEFENSIVE

7. Defence service manpower sufficient for commitments?

Yes. And numbers have been increased since Cmnd 8288 to take account of commitments in the South Atlantic.

8. Correct balance between 'teeth' and 'tail'?

Yes. The MOD is always seeking to increase the efficiency of support areas to allow strengthening of the front line.

LOCAL AUTHORITIES

DEFENSIVE

9. Local authority manpower still too high?

Manpower reductions are a key to reducing local authority spending. The recent rise in manpower is therefore very disappointing and must be reversed.

NATIONAL HEALTH SERVICE

POSITIVE

10. Size and efficiency?

- (i) The government has settled manpower targets with Regional Health Authorities, providing for a reduction of 4,800 staff ($\frac{1}{2}$ per cent) between March 1983 and March 1984.
- (ii) New arrangements have been introduced from 1984-85 whereby manpower control is to be central feature of health authority short-term programmes and an integral part of overall planning. Authorities are expected to ensure manpower targets are consistent with service objectives and cash available. Any unsatisfactory plans will be rejected.
- (iii) The NHS Management Inquiry on effective use and management of manpower and related resources in the NHS reported in October 1973 and the general thrust of the report has been accepted.
- (iv) All health authorities are required to carry through a substantial and sustained cost improvement programme which will make services more efficient and release resources for improvements and new developments. Any plans omitting such a programme will be rejected.
- (v) The government is urging health authorities to contract out services to the private sector wherever it would be economical to do so (from 1 September 1983 VAT relief will be available when this occurs).

DEFENSIVE

11. Are manpower control arrangements for 1984-85 not reversal of last year's manpower targets policy?

No. The 1983 targets were a necessary response to failure by authorities to secure adequate

manpower control. The new arrangements are the intended longer term outcome to the wider manpower exercise launched 2 years ago.

Fact Sheet - Key Comparisons

Civil Service Manpower

<u>Date</u>	<u>Number</u>	<u>% Reduction</u>
1.4.79	732,300	-
1.4.82	666,400	9%
1.4.83	648,912	11%
1.1.84	632,600	13.6%
1.4.84	630,000 (estimate)	14%
1.4.85	608,208 (estimate)	17%
1.4.88	*593,00 (estimate)	19%

*6% reduction over 1.4.84 figure of 630,000

OUTPUT MEASURES

(Note: this brief refers to many examples of output measures published for the first time in a public expenditure white paper. Some have, of course, been published in other places before).

1. What are they and why include them?

Output measures describe what is produced by public expenditure. They show the public, especially taxpayers, what they get for their money. These basic facts are essential for informed debate about public expenditure.

2. More measures this year?

Yes. This white paper includes about 550 output measures; an increase of about 40 per cent on Cmnd 8789.

For the first time every programme includes some output measures. (Note: the local authority section has none, but some LA outputs are quoted under central government programmes).

For example the Northern Ireland section includes output measures covering well over 90 per cent of expenditure. Measures not published in previous white papers include the number of farmers participating in agricultural advisory programmes and improvements in milk yield and silage production, kilometres of watercourses built and maintained, a target to reduce unfit housing by 1 per cent per year, numbers of public sector improvements to housing and grants and a range of health service activity statistics.

3. A few of the other new measures are:

- a) Research sponsored by MAFF has demonstrated how to achieve savings in distribution of tomatoes that should amount to 2 per cent of the value of home production;
- b) projects for over 3,000 hostel beds have been approved by the Housing Corporation;
- c) the other environmental services section quotes occupancy rates for advance

factories built by the Development Commission.

4. Better measures this year?

Yes. Careful comparison shows most programmes quote better, as well as more, measures. A few examples:

- a) the value of the trunk roads programmes to the public has been published before, as a benefit: cost ratio. For the first time this white paper quotes some measures of environmental disturbance - namely dwellings affected by noise - that is not included in the cost benefit analysis;
- b) some details like the increase in employment in Assisted Areas as a result of regional policy, are included for the first time;
- c) more measures, including the number of miles of motorway and other trunk road constructed, and the numbers of people covered by sheltered employment schemes, now describe a run of years so that trends can be seen;
- d) the Energy programme includes some precise planned outputs, or targets, for power output from nuclear reactors;
- e) the urban programme and Scottish sections describe how public sector investment 'levers' private sector investment in certain cases.

5. Why not more?

Space is limited. The bibliographies at the end of each section include references to other sources for output measures. Some measures, especially in the Defence area, should not be published for national security reasons.

6. Why not better?

Output measurement is technically difficult. For example the Education section quotes improvements in examination results, while saying this is only a limited measure of progress. At the moment it is not surprising that most output measures describe physical levels of activity or provision. Improvements will continue, eg under FMI, the Treasury will continue to encourage these developments and when suitable measures are developed they can be presented in the white paper. For example the Urban Programme section includes a commitment to develop suitable measures within two years.

includes a commitment to develop suitable measures within two years.

7. Output and volume

Output measures are much better than the old volume figures because they show what the public is getting. Volume figures can only show the value of expenditure to the public in two special circumstances: when a programme has only one output or when the price paid by government for all outputs is in direct proportion to their value to the public. These circumstances rarely, if ever, apply.

8. Output and cost terms/cash

Obtaining maximum output from the cash available depends on good planning improving efficiency and on keeping price rises as low as possible. The Transport section includes a discussion of the factors affecting output.

PUBLIC SERVICE PAY AND PENSIONS

O1. How realistic are the Government's pay factors - past and present?

These assumptions are used to plan public expenditure. They do not relate to any individual pay settlement. Settlements higher, or lower, than 3 per cent are not ruled out. We believe the 3 per cent provision for 1984-85 is a reasonable one overall. [If pressed: In 1983-84 a 3½ per cent assumption did not preclude a settlement of 4.86 per cent for the Civil Service, 4 per cent for the NHS etc.]

O2. But 3 per cent is low compared with pay settlements in this round - how will it be made to stick?

The Government intends to have genuine negotiations on pay. These will take account of a number of factors, including cost. 3 per cent is an important indication of cost considerations.

O3. What if pay awards cannot be financed from within the estimated provision? Will there be manpower implications?

As in previous years the presumption is that the additional cost of any settlement above 3 per cent would be found from within the existing provision. To the extent that there are pressures for higher rates of increase, the question of the trade off between pay and jobs must inevitably start to come into focus. [If necessary: But recourse to the Contingency Reserve is not absolutely ruled out.]

O4. Provision in the plans for pay in the later years and the future of the pay factor

The practice of setting future plans in cash terms is now firmly established. No specific assumptions for pay are incorporated in the figures for the later years. It will be for consideration whether to announce a specific pay factor for 1985-86 later this year.

Q5. What is the redundancy cost of the planned rundown in Civil Service numbers?

In general we expect to achieve the rundown to 1988 by natural wastage although there may be a small number of redundancies. Where staff are transferred with their work out of the Civil Service terms and conditions will usually be no less favourable and redundancy compensation will not be paid.

Q6. What assumptions have been made about employees' pensions contributions, in view of the manifesto commitment to ensure that they are 'realistic'?

The PEWP pay figures are based on current contribution levels - ie, the non-contributory civil service and armed forces schemes, 5/6 per cent in the large, normal accrual schemes (teachers, local government, NHS), and 11 per cent for police and firemen. The Government remains committed to the policy of ensuring that public sector employees make realistic contributions towards their index-linked pensions.

DEFENCE

£ million	<u>1983-84</u>	<u>1984-85</u>	<u>1985-86</u>	<u>1986-87</u>
Cmnd 8789	15987	17290	18330	
net difference	-271	-259	-270	
Cmnd 9143	15716	17031	18060	18660
of which Falklands	624	684	552	450

POSITIVE1. Defence budget growing

Provision up to 1985-86 meets the NATO aim of 3 per cent real growth per annum, with Falklands costs on top.

2. Size of defence budget

Defence is the second highest public expenditure programme. The UK defence budget is the second highest in NATO. As a proportion of GDP and per capita, it surpasses all our major European allies.

3. Cost terms growth in defence

In cost terms, the 1984-85 Falklands- inclusive defence budget will be over 26 per cent higher than in 1978-79 (some 22 per cent higher Falklands-exclusive) - table 1.14 of Part I.

DEFENSIVE4. Limit to 3 per cent commitment

The commitment to plan for annual real growth of 3 per cent has not been extended beyond 1985-86. By then, the defence budget will have increased in real terms every year for seven successive years. The 1986-87 defence budget, Falklands-exclusive, will be some 4 per cent (£700m) higher than the previous year, with an addition for Falklands expenditure.

5. Reductions since Cmnd 8789

The reductions from Cmnd 8789 provision take into account the March 1983 NIS reduction, the 3 per cent public service pay assumption for 1984-85, and the 1983-84 cash limit cut.

6. Reasons for £21 million increase since Autumn Statement

1984-85 provision of £17,031 is higher than the autumn statement figures of £17,010 owing to transfers from D/Employment to meet the cost of defence Youth Training Scheme, the transfer of COI services to repayment basis, and an adjustment to the charging basis for fishing protection. There is no net increase in public expenditure.

7. Falklands

Provision over the period is some £2300 million (£3100 million including £780 million in 1982-83). Provision up to 1985-86 was announced in Cmnd 8789. The declining trend reflects the phasing of expenditure on capital facilities for the garrison and on the replacement of equipment losses.

8. Manpower

A target for civilian numbers has been set of 170,000 at 1 April 1988. This compares with 200,000 civilian personnel at 1 April this year.

EUROPEAN COMMUNITIESFACTUAL

NET PAYMENT TO EUROPEAN COMMUNITY INSTITUTIONS (EXCL. OVERSEAS AID)

1978-79	1979-80	1980-81	1981-82	1982-83	1983-84	1984-85	1985-86	1986-87
751	839	221	153	580	500	375	550	600

1. Are our net payments to Community institutions the same as our net contribution to the Community Budget?

No. The figures shown in the White Paper reflect the net Public Sector cash flow from the UK to the EEC Budget together with adjustments in respect of the European Investment Bank; European Coal and Steel Community and overseas aid. Our net contribution is the difference between our gross payments and our gross receipts (ie. both public and private sector).

POSITIVE

2. Net payments: how certain are the figures?

Net payments figures fluctuate considerably from year to year. They are subject to a wide variety of uncertainties, for example, UK and EEC imports and import prices (which affect our budget contributions) and the future pattern of expenditure in the Community budget (which affects our budget receipts).

The projections also depend on the stylised assumptions about our budget refunds (see further below), and an assumption about the growth of the Community budget. These matters are the subject of negotiations within the Community.

3. What are the assumptions on refunds?

In respect of 1984 and later years, it has been assumed that the UK will receive a net refund equal to about two thirds of our net contribution to the "allocated" budget (this excludes

expenditure on overseas aid, refunds and certain other items). This is a stylised assumption, and not a forecast nor a negotiating objective. It is assumed that the bulk of the refunds will be paid by 31 March in the year following that in which they arise.

A refund equivalent to two thirds of our net contribution to the allocated budget is what the UK actually achieved on average over the four years 1980 to 1983. [The net refund is grossed up to ensure that the UK does not pay towards either its own refunds or the German compensation towards their share of the refunds].

DEFENSIVE

4. What if refunds are not paid by 31 March?

The Government expects that the bulk of the refunds agreed at the Stuttgart European Council will be paid by the end of March. The Prime Minister has stated that if they are not received then we shall have to take steps to safeguard our position. Slippage of our refunds from 1983-84 to 1984-85 would increase public expenditure in 1983-84 and reduce it in 1984-85 by an equivalent amount.

5. Net payment figure for 1984-85 drops to £375 million - why?

The fall in 1984-85 reflects a number of factors. On the basis of the exchange rate assumptions used in constructing the projection, our VAT payments in 1984-85 are likely to be somewhat depressed. We are also assuming a larger refund in respect of 1984 than that agreed at the Stuttgart Council in respect of 1983. The 1984 refund reflects the stylised assumption used for future years. The refund in respect of 1983 agreed at Stuttgart took account of the relatively favourable refund payments received in 1980 and 1981.

6. The figures are on an upward trend. Is the Government concerned about this?

The projections are uncertain for the reasons given. The Government is concerned that our corrected net contribution to the Community Budget should be at level which is fair. To this end, it has proposed that a "safety net" ought to be introduced, which would limit our corrected net contribution to our ability to pay, as measured by relative prosperity. This is currently the subject of negotiation within the Community.

7. What has been assumed about the payment of the £42 million risk-sharing money?

This money should have been included in the 1983 Community Budget. The projections

assume that it will be paid by the end of March 1984. The Foreign Secretary has written to Mr Thorn, President of the Commission, requesting payment. We are awaiting his reply.

8. Why do the UK's receipts level off from 1984-85?

This is the result of the assumption that 1 per cent own resources ceiling is maintained, which has the effect of levelling off the size of the total Budget and with it, our receipts and contributions.

9. What about milk disallowance?

The Commission have decided against disallowance of 1978 and 1979 expenditure on milk. The question of disallowing expenditure in later years has not yet arisen. We see no case for it. The Commission have not withdrawn their authorisation of the Milk Marketing Boards.

PM Statement in HOC on 31 January 1983. "We would regard it as absolutely intolerable if the Commission were to try to disallow this expenditure. It would be without precedent and would not be justified in any way. The Commission have authorised the Milk Marketing Boards under the rules laid down, and have not attempted to withdraw that authorisation".

MAKE CLEAR: THERE IS NO CONNECTION WITH UK REFUNDS.

AGRICULTURE/IBAP

1. Cuts in MAFF spending

MAFF expenditure has been reduced below Cmnd 8789 totals by £13 million in 1984-85 and £33 million 1985-86. The cuts have mainly fallen on agricultural capital grants.

Agriculture cannot be exempt from Government policy on public expenditure.

2. Increases in IBAP spending

There are substantial increases in IBAP's expenditure over the totals in Cmnd 8789 (£413 million in 1984-85 and £233 million in 1985-86). This represents expenditure by IBAP on agricultural support under the CAP. About one third of the increase is for expenditure which is pre-funded from the Community Budget. The rest reflects forecast extra intervention purchases, particularly for milk products: these costs fall initially on the Exchequer but are recouped from sales and by Community reimbursement for losses when intervention stocks are sold.

3. IBAP increases demonstrate Government does not want to reform CAP

The increases reflect the latest forecast of the cost of implementing existing CAP policies. Forecasts are highly uncertain as they depend on assumptions made about the weather, Community harvests and world market conditions. Common prudence to include up to date forecasts for such expenditure. Current trends emphasise the importance of Government's policy of pressing vigorously for reform of CAP and for a strict guideline for CAP expenditure.

4. What about milk disallowance?

The Commission have decided against disallowance of 1978 and 1979 expenditure on milk.

PM Statement in HOC on 31 January 1983. "We would regard it as absolutely intolerable if the Commission were to try to disallow this expenditure. It would be without precedent and would not be justified in any way. The Commission have authorised the Milk Marketing Boards under the rules laid down, and have not attempted to withdraw that authorisation".

HOUSING (England)FACTUAL

		1984-85	1985-86	£bn 1986-87
Net provision	2.8	2.5	2.6	2.7
	1.5	1.6		
Gross provision	<u>4.3</u>	4.1	na'	na'

'receipts assumed to be at least £1.3bn (after £1.6bn in 1984-85).

POSITIVE1. Comparison with 1983-84 provision in Cmnd 8789

The gross provision for capital expenditure for 1984-85 on housing is the same as that provided for 1983-84 in Cmnd 8789. Receipts are now expected to be £200 million higher and the provision for current expenditure is £100 million lower than the provision for 1983-84 in Cmnd 8789

2. What is happening to capital expenditure

The gross provision for capital expenditure in 1984-85 is about the same as for 1983-84. But the outturn for local authority gross capital expenditure is expected to be some £300 million above provision. But receipts are even higher above plan so it is likely that the new end-year flexibility scheme will give local authorities a provision for capital spending some £29 million above that shown in Cmnd 9143.

3. Private Sector

Private sector housing starts in 1983 the highest since 1973.

DEFENSIVE4. Reductions: Effects on construction industry.

The 1984-85 cash provision for gross capital expenditure, the significant element in the

total for the construction industry, is broadly the same as for 1983-84.

5. Ending of temporary Home Improvement Grant measures.

These measures, introduced in the 1982 Budget, were clearly stated by the then Chancellor to be temporary measures designed to take up immediate capacity in the construction industry and not to add to longer term demands on it. The original deadline for applications was twice extended and has now been confirmed as 31 March 1984.

6. Local authority capital allocations. Amount available for particular items.

The total available for allocation is broadly the same as last year. Individual authorities are free to determine their priorities for capital expenditure within their total.

7. Lack of forward planning

Local authorities were promised at least 80 per cent of their 1983-84 allocations in 1984-85 and that undertaking has been honoured. For 1985-86 and 1986-87 local authorities have been promised 80 per cent and 70 per cent respectively of their 1984-85 allocation.

8. Capital underspending by local authorities.

Although net underspending in 1983-84 is some £200 million, gross expenditure by local authorities (ie before deducting receipts) is likely to be some £250 million above provision mainly because of increased spending on home improvement grants.

SUPPORT FOR INDUSTRY

1. Why is Support for Industry falling?

The DTI's budget (excluding nationalised industry EFL's) falls from £1578 million in 1983-84 to £1360 million in 1984-85. This is largely because no provision is made for BL in 1984-85 after a £150 million provision in 1983-84. BL is expected to be independent of Government finance after this financial year.

2. What about subsequent years?

The DTI budget (excluding nationalised industry EFLs) is fairly constant after 1984-85 with a provision of £1300 million in 1985-86 and £1270 million in 1986-87.

3. What are the main changes within the DTI provision?

Support on industrial research and development and innovation continues to increase, reflecting the high priority the Government gives to promoting technological advance to enable industry to improve its international competitiveness. Assistance towards shipbuilding and steel redundancies tapers off over the Survey period as the restructuring of these industries is completed. There is also a reduction in assistance to Rolls Royce, reflecting the end of the RB 211 development stage.

4. Do these figures include the effects of the proposed regional policy changes?

No. The figures will be adjusted in the course of the year when Ministers have taken decisions about rate of grant and the new assisted area map. Substantial savings are expected.

5. How much will the regional policy changes save?

Too early to say.

6. Do the figure include launch aid for the A 320 and V2500?

No. Ministers have decided in principle to provide some launch aid towards the V2500 engine but the figure has yet to be settled. Discussions continue with British Aerospace about the A320.

7. Why has Concorde fallen to zero?

Because the Government plans to transfer responsibility for the in-service support of Concorde to British Airways from April 1984.

HEALTH

POSITIVE

1. Comparison with last year's plans

Planned spending on the NHS is up on the plans in last year's White Paper.

£m	1984-85	1985-86
New plan	13138	13860
Old plan	13130	13710

2. Meeting costs of demographic change

The new plans imply growth in resources of about 1 per cent a year - double the long-term planning assumption - and sufficient to cover full costs arising from growing numbers of old and very old people.

3. Consistent with Election Pledges

The new plans are for spending £845m more in 1984-85 than in 1983-84, and for £877m more in 1985-86 than in 1984-85. This rate of increase more than fulfils the Prime Minister's Edinburgh speech (figures: £800m and £700m respectively). [Note: these are figures for health spending Great Britain which cannot be calculated from the White Paper tables.]

4. Efficiency

The NHS is being expected to bring forward major efficiency savings to provide for improvements in services and to reduce waiting lists. The Griffiths report recommends

ways of transforming the management of the NHS and will make it much easier to secure such savings. The Government is requiring each health authority to devise a substantial cost improvement programme.

5. Achievements

Since coming into office the Government has:

- doubled health spending: an increase 17% above the RPI
- increased health services by over 7 per cent

Results shown in White Paper:eg -

- ½ million more in-patient day cases
- nearly ½ million more people visited at home by Health visitors and District nurses
- 2½ million more courses of dental treatment

DEFENSIVE

6. Prescription charge going up?

Changes in charges will be announced by Social Services Secretary, but the exemptions from charges will remain. [Note: Mr Fowler has not yet decided when to announce new levels of charges.]

7. 1984-85 plan based on unreal pay assumption?

The Government announced on 5 September that it was making provision of 3 per cent (in its cash plans) for pay increases within central government, but that this did not predetermine

any individual settlement. Fruitless to speculate on what action might be taken if NHS settlements next year turn out at a difference figures.

8. Government not funding costs of new medical technology

Reasonable to look to improved efficiency and cost reduction to offset the costs which can arise from advances in medical science. Many medical advances actually reduce costs (eg drugs which allow the mentally ill to be treated at home rather than in long-stay institutions).

[Background: some people estimate costs of medical advance to be $\frac{1}{2}$ % a year but there is no sound basis for any such figure].

9. Manpower cuts damage NHS

Nonsense to suggest a big organisation like the NHS cannot stand manpower cuts of just $\frac{1}{2}$ %. Government had to act because of clear evidence that health authorities had failed to get a grip on their manpower. For the future health authorities have been asked to merge their plans for manpower with their plans for services. As efficiency increases services will rise faster than resources, and resources by more than manpower.

SOCIAL SECURITY

1. Changes since CMND 8789

Plans show increases of about £1300 million in 1984-85 and £1600 million in 1985-86. Reasons include effects of the 1983 benefit improvements in uprating, (including 11 per cent increase in child benefit and one-parent benefit), and effects of changes in uprating assumptions slightly offset by lower unemployment assumptions. Together these add about £600 million in 1984-85 and £850 million in 1985-86. Another factor is revised estimates of expenditure on certain benefits including supplementary benefit, associated with a higher number of beneficiaries than previously estimated, and housing benefit. These are partly offset by lower estimates of expenditure on unemployment benefit. Modified proposals for reductions in the coverage of help with housing costs were announced by the Secretary of State for Social Services on 6 February.

2. Changes since Autumn Statement

Plans for 1984-85 show an increase of about £360 million because of revised estimates (based on later information) of expenditure on benefits, mainly supplementary benefits. The increase is being met from the reserve.

3. Provision for Uprating

Programme provides for upratings in November based on rise in prices in the year ending in the previous May. Actual decisions on benefit levels will normally be announced by Secretary of State for Social Services in June of each year. (The projections assume that the retail price index will rise by 5½ per cent in the 12 months to May 1984 and by 4½ per cent and 4 per cent respectively in the subsequent two years).

4. Government Pledges to Maintain Value

The Government is committed to its pledge (renewed in the Election Manifesto) to maintain the value of pensions and linked long-term benefits.

5. Child Benefit Uprating

The decision on the level of child benefit from November 1984 will be taken in the light of all relevant circumstances and announced at the appropriate time. (Meanwhile, provision in

the programme is, by convention, based on the uprating assumptions for pensions and linked long-term benefits.

6. Expenditure still growing

Social security expenditure is assumed to grow by about £2 billion in each of the three years 1984-85 to 1986-87. About half of this growth is expenditure on pensions (about £750 million in 1984-85 and just over £1 billion in each of the following two years).

7. New Benefit

The severe disablement allowance will, subject to passage of the Health and Social Security Bill, be introduced from November 1984 at an initial cost when fully phased in of about £20 million for a full year. It will replace the non-contributory invalidity pension and housewives' non-contributory invalidity pension.

8. Housing Benefit cuts

Why are cuts necessary?

Some economies have to be made in Social Security programme if overall public expenditure is to be contained. Reasonable to look for some offset to ever-increasing cost of paying for benefits. Housing benefit currently goes to 7 million households 1 in 3. Goes higher up the income ladder than any other means tested benefit. Some recipients have above average income. Better to make savings there than on means tested safety net.

9. Government has backed down on housing benefit cuts?

Government still believes it is right to make economies in this area. In particular, Government considers it perfectly reasonable to expect those who are working to make a contribution to housing costs (largest losses are among families with working teenagers). Modifications announced on 6 February are to ease particular problems identified by Social Services Advisory Committee and give local authorities more time to deal with administrative task of implementing changes.

10. Effect of changes

The modifications will soften the impact of the changes for 1,300,000 households. 300,000 who would have lost all benefit in April will now not do so (NB. some of them may lose all

benefit in November). In April, over half of claimants will face losses of under 50p a week. 81 per cent (89 per cent pensioners) will face losses of under £1. Those facing larger losses (mainly better off families with working teenagers) will have longer to adjust.

11. Cost of concessions

Cost of concessions put at £45 million in 1984-85 and about £15 million in 1985-86 but that does not all count as public expenditure. (Help with rates does not). The public expenditure cost will be contained within the published plans.

[If pressed - some of the cost is being met by postponing the planned real increase in children's needs allowance. Part (£8 million in 1984-85, £3 million in 1985-86) is being met from the reserve. The rest will be met by savings in the social security programme.]

LOCAL AUTHORITY CURRENT EXPENDITURE AND RATE SUPPORT GRANTDEFENSIVE1. Provision inadequate?

No. Represents a £600m increase over provision underlying last year's White Paper, to take account of overspending by local authorities of 1983-84 provision. Cash standstill over 1983-84 budgets - but they are too high. Targets set consistent with that provision allow authorities which have kept spending down a 3 per cent increase over budgets; authorities which have failed to meet previous targets, faced with maximum 6 per cent cash cut (except GLC); key to what targets mean for services lies with authorities' ability to control own costs.

2. Grant settlement means high rate rises?

No. All depends on local authority spending decisions. AEG before holdback £100m higher than in 1983-84. Stiffer penalties in England and Wales: but no authority meeting its targets will lose grant through holdback. No need for there to be excessive rate increases if authorities budget sensibly.

3. Expenditure savings from rate capping in 1985-86?

Selective rate limitation scheme will operate in 1985-86. The first 12-20 authorities will be selected once Parliament enacts the Rate Bill. Capping the highest spenders will mean expenditure savings. Operation of rate capping powers will enable target/penalty system to be fairer on those authorities who have kept spending down (cf commitment given by Messrs Jenkin and Waldegrave in the RSG Debate on 23 January). [Not for use: provision agreed for 1985-86 takes no specific account of impact of rate capping].

4. Rationale for unallocated margin throughout survey period

Unallocated margin reflects expenditure that government realises is inevitable, in light of authorities' past spending performance but considers undesirable. Local authorities' past spending record suggests that they will not reduce their spending level to the levels the government considers desirable over the Survey period.

5. Government wrong to accuse LAs of excessive spending?

No. Local authority current spending has gone up well ahead of increase in general level of prices since 1978-89, despite government urging restraint. Capital and current together have gone down as a percentage of GDP, because of very large fall in net capital spending i.e after taking off council house sales.

LOCAL AUTHORITY CAPITAL SPENDING

POSITIVE

1. What is the level of LA capital spending?

Provision for LA capital in 1984-85 (GB) is almost £3.7 billion, which is about the same level of spending as that forecast as the outturn for 1983-84.

2. Has the high level of underspending seen in LA capital over the past few years been repeated in 1983-84?

The high level of underspending which has been a feature of LA capital over the past few years seems unlikely to be repeated this year. The latest forecast outturn for 1983-84 indicates that local authorities will be within £250 million, or about 7 per cent, of the levels given in the last White Paper (£3.9 million).

3. What steps have the Government taken to help local authorities plan their capital programmes?

Once again the government has given local authorities guidance about the likely level of future allocation. (Plans for 1985-86 for education, transport and social services are indicated in the programme tables; for housing and local environmental services, subject to some conditions, local authorities have been told that their allocations for 1985-86 will be at least 80 per cent of 1984-85 levels.) Additionally, for the first time and where applicable, there is to be a system of end year flexibility on the national cash limits which will allow some underspending to be carried forward into the next financial year.

DEFENSIVE

4. Why does table 2.18 show LA capital falling between 1983-84 and 1984-85?

Although the plans show a fall of about £200 million between 1983-84 and 1984-85 it must be remembered that the figures are net of receipts. If receipts are allowed for, the gross spending between these two years is planned to rise from £5.8 billion in 1983-84 to £6.6 billion in 1984-85.

5. Will the rates limitation cause capital spending to be restricted?

In determining the rates limit local authorities overall spending will be looked at in detail. This means that the limit will be set with reference to both capital and current spending. Since it is current spending we wish to see reduced we would hope that capital spending continues at its planned level.

6. Will the rates limitation legislation bring into question the creditworthiness of LA's and cause them to default on their loans?

No. Concern about creditworthiness is utterly unfounded. It is true that English legislation does not describe lending as a first charge on an authority's revenues. But it is specified as being a charge - and since it is the only liability so specified anywhere in the whole of English legislation on local government the charge is in effect a first charge. [A more detailed brief is attached at C4].

NATIONALISED INDUSTRIES1. What has happened to Nationalised Industry External Finance since Cmnd 8789?

	£m			
	<u>1983-84</u>	<u>1884-85</u>	<u>1985-86</u>	<u>1986-87</u>
Cmnd 8789*	2290	2615	2145	-
Cmnd	2250	1881	1145	91
Difference	- 490	- 734	-1000	-

*With figures added for the water industry (England and Wales) which is included for the first time this year in the nationalised industries section of White Paper.

A marked strengthening in industries' position therefore shown over the forward look period.

2. Does the fall in External Finance in future years represent a tightening Government screw on the Industries?

Not in that sense. The marked fall in industries' expected need for external finance in future years, largely arises from further cost and performance improvements.

3. What assumptions are made about British Airways and British Telecom?

EFLs for BT and BA are included in 1984-85 for sake of consistency with Autumn Statement. These EFLs are subject to great uncertainty because of impending privatisation. No more detailed breakdown of these figures is given in the White Paper Tables. Remains Government's stated position that the sale of British Telecom is planned for next autumn with British Airways in early 1985.

4. Are financial plans realistic?

Plans based on comprehensive reviews of industries' requirements. But depend on industries keeping current costs, including wage costs, under control in the way that private sector

companies have to do. Failure to do this is likely to mean either higher prices or less investment. No evidence that plans are unrealistic.

5. Is industries' investment currently at a satisfactory level?

Yes. In fact

(a) allowing for privatisation and a change in BT's accounting treatment of fixed assets, industries' expenditure on fixed assets in 1982-83 increased by 7 per cent over 1981-82; and

(b) again allowing for privatisation, investment in 1983-84 is expected to show a 12 per cent increase over 1982-83 and to be much closer than in previous years to the industries' plans.

6. Do not future years show a drastic fall in industries' projected investment?

Not at all. The marked fall in industries' investment between 1983-84 and 1984-85 and subsequent years reflects the expected privatisation of British Telecom, British Airways and Enterprise Oil and the exclusion of their figures from the Nationalised Industries totals. Investment by these industries will of course take place in the private sector to the full extent that it can be justified on commercial grounds.

7. What does all this mean for prices?

Industry tariffs in 1984-85 are expected to rise at, or slightly below the rate of increase in the RPI.

8. What about the recent debate over electricity prices?

The Government suggested a 2 per cent increase in April to give confidence that the electricity supply industry would meet its EFL (-£750 million) and to avoid the risk of sudden large increases later. This rise is consistent with economic pricing and is lower than expected when the present financial target (a low 1.4 per cent return on assets to March 1985) was set a year ago.

9. Does not the rapidly decreasing external financial figures for the nationalised industries in futue years imply massive gas/ electricity price increases?

Not at all. No connection can be drawn with price levels in any one industry. Gas and electricity prices for future years have still to be settled.

SPECIAL SALES OF ASSETS1. What changes in outturn/targets have taken place since Cmnd 8789?

	£m cash					
	<u>1981-82</u>	<u>1982-83</u>	<u>1983-84</u>	<u>1984-85</u>	<u>1985-86</u>	<u>1986-87</u>
Cmnd 8789	+ 79	- 550	- 750	-1500	- 500	-
Cmnd	+ 70	- 488	-1200	-1900	-2000	-2000
Difference	-	+ 62	- 450	- 400	-1500	-

Changes since Cmnd 8789 reflect decisions on privatisation since last targets published and make allowance for additional disposals arising from the continuing scrutiny of potential candidates for privatisation. Target of £1.9 billion asset sales in 1984-85 previously announced in the Autumn Statement.

2. What is latest position on British Telecom (BT) and British Airways (BA) impending privatisations?

There is nothing to add to the Government's stated position that the sale of British Telecom is planned for next autumn with British Airways in early 1985.

3. What do future year asset sales targets imply for method of BT sale

No final decision has yet been taken on the method of BT sale. Always genuine uncertainty about level of receipts but level of £1.9 billion in 1984-85 and £2 billion per annum in 1985-86 and 1986-87 is realistic and achievable target.

[NOTE: You will not wish to be drawn any further on any apparent connection between the method of BT sale and target figures for 1984-85 and future years].

4. What individual sales are included in the 1983-84 estimated outturn?

Sales this year include those of further BP (£540 million) and Cable and Wireless (£262 million) shares and receipt of second instalment (£293 million) from earlier Britoil

share sale. The estimated outturn of -£1200 million compares with a target of -£750 million at the time of the 1983 White Paper, itself subsequently revised to -£1250 million. Full details of this year's receipts will be published after the end of the financial year.

5. Is Wytch Farm included in the 1983-84 figures?

Yes. We are continuing to look for completion of the first stage of the Wytch Farm disposals this year.

What are future privatisation plans?

Exact shape of programme in future years will be determined by market and commercial considerations and commonsense. Not practice to reveal composition of future asset sales programmes but will be consistent with Manifesto commitment.

7. What is included in "Special Sales of Assets"?

Special Sales of Assets record those privatisation receipts that are treated as negative public expenditure within the planning total. Receipts that are retained by nationalised industries or within Departmental programmes are not included.

8. Are not higher targets just a covert way of financing PSBR?

No. Any cash income is naturally welcome as is the future reduction in interest payments from a lower PSBR. But the Government's aim in its privatisation programme is to increase competition and promote efficiency. This benefits the economy as a whole.

9. Effect of higher asset sales on public expenditure

The receipts from assets sales reduce net public expenditure in the same way as purchase of capital assets increase expenditure. The receipts help to reduce the pressure on other types of public expenditure.

10. Will not higher asset sale targets in future years cause capacity problems in the UK financial targets?

No reason to believe this will be so. 1983 UK listed company capital issues in London were 50 per cent higher than even before. The nature of privatisation shares is such that, in any event, investors are likely to want to adjust the balance of their portfolios in order to accommodate them.

DEBT INTEREST1. Changes since Cmnd 8789?

	£ million			
	<u>1982-83</u>	<u>1983-84</u>	<u>1984-85</u>	<u>1985-86</u>
<u>Gross Debt Interest</u>				
Cmnd 9143	15580	15500	15500	15500
Cmnd 8789	14750	14750	14750	14750
Change	830	750	750	750
<u>Net Debt Interest</u>				
Cmnd 9143	5946	7000	7500	7500
Cmnd 8789	6000	6500	6500	6500
Change	-54	500	1000	1000

Revisions to gross debt interest are due to a number of factors. These include revisions to the CSO's outturn figures, higher than expected borrowing in 1982-83 and 1983-84, higher expenditure on interest support costs and higher interest payments by public corporations to the private sector and overseas. It is not the case that the underlying interest rate assumptions have been increased.

The revisions to net debt interest (which were mostly anticipated in the public expenditure/GDP percentages in the Autumn Statement) do not follow those to 'gross' one-to-one because of variable effects on the adjustments subtracted from 'gross' to obtain 'net'. (The adjustments are general government interest receipts, interest provision in general government trading activities, interest support costs and public corporations payments to the private sector and overseas.) For 1982-83 the revision to gross is more than offset by revisions to each of the adjustment components, all working in the same direction. Detailed forecasts of the adjustment components are not published because to do so would indicate spurious accuracy.

2. Flat path for gross debt interest for forward years?

Flat path reflects broad expectation that effects of additional public sector borrowing (ie a positive PSBR) will be offset by lower interest rates, leaving overall interest payments unchanged.

[IF PRESSED on interest rates assumed: Precise interest rate assumptions are not published because they are market sensitive, but path indicated is consistent with a steady decline.]

3. Large rise in net debt interest in 1983-84?

[Gross debt interest likely to change little in 1983-84 compared with 1982-83; net figure shows projected increase of about £1 billion.]

Debt interest gross is little changed, lower interest rates being offset by the increasing stock of debt. On interest receipts (and on the other adjustments to "net") the full effect of the interest rate falls comes through, causing the net amount of debt interest to be financed by taxation and further borrowing to rise. [Cmnd 8789 also showed net debt interest increasing in 1983-84 with gross staying flat.]

4. Any significance in path for servicing of index-linked securities?

Servicing of indexed linked securities

	£ million				
	1982-83	1983-84	1984-85	1985-86	1986-87
Cmnd 9143	865	750	1000	1050	1150
Cmnd 8789	800	750	900	950	..
Change	65	-	100	100	..

a. Main reason for dip in 1983-84 is the reduction in the rate of inflation affecting the uplift on index-linked gilts and National Savings certificates, as anticipated in Cmnd 8789.

b. In 1984-85, servicing of index-linked gilts rises due mainly to the effects of substantial new issues in 1983-84, again mostly anticipated in Cmnd 8789.

SPRING SUPPLEMENTARY ESTIMATES

66 Spring Supplementary Estimates for a total of £1313 million are being presented at 2.30pm on 16 February, one hour before your press conference on the White Paper. A copy of the press notice on the Supplementaries is attached.

1. Do the White Paper figures take account of the Spring Supplementaries

Although the detailed figures for these Supplementaries have been finalised after it was necessary to "close the books" for the White Paper their general level was anticipated in and is consistent with the estimated aggregate public expenditure outturn for 1983-84 shown in the White Paper.

2. How do the Spring Supplementaries affect programmes and the Contingency Reserve

Of the £1313 million extra provision represented by these Supplementaries, £296 million is not classified as public expenditure (eg transactions within the public sector). The remaining £1017 million is made up as follows:-

(a) Offset by savings within existing totals:	£498 million
(b) Charged to the Contingency Reserve within the planning total:	£128 million
(c) New public expenditure from demand-led programmes:	£391 million.

3. What are the main Spring Supplementaries

The largest Supplementaries all concern demand-led programmes. They are:-

(i) £289 million on support to the coal industry	(Class IV,3)
(ii) £213 million on Supplementary benefits	(Class XII,2)
(iii) £169 million on housing benefits	(Class XII, 4)
(iv) £168 million on housing grants	(Class VII,1)

4. These figures include substantial offsets within existing planning totals.

Cash limits

All substantive changes to cash limits have been announced to Parliament.

5. Treasury Supplementary Estimates

Questions on individual Supplementaries and cash limits should be directed to the

department concerned. Two Supplementaries fall within the responsibility of Treasury Ministers:-

- (i) Class IV, Vote 26 covers the recent sale of shares in Cable and Wireless plc and is for a token £1000 as receipts a outstrip expenditure.
- (ii) Class XIII, Vote 7 (Inland Revenue) seeks £10 million extra provision for relief on life insurance premiums and mortgage interest charges, following changes in interest rates and revised tax thresholds since the main Estimate was presented last March.

6. Comparison with Spring Supplementaries in previous years.

The extra provision sought this spring is lower than that for the corresponding period in each of the past 3 years. The figures are as follows:

	<u>£ million</u>
1980-81	2165
1981-82	1459
1982-83	1587
1983-84	1313

7. Outturn on Estimates

7. The final outturn of Supply Expenditure will differ from the total of Estimates presented so far because there will inevitably be some underspend on votes. The pattern over recent years has been:

	<u>£ million</u>		
	<u>Total voted</u>	<u>Outturn</u>	<u>Saving</u>
1980-81	69,234	67,637	1,597
1981-82	76,290	74,273	1,997
1982-83	82,682	80,605	2,077

BACKGROUND NOTE: 1983-84 OUTTURN

The planning total figure of £120.3 billion in the White Paper is arrived at by adding up departmental returns of their latest estimate of outturns on spending programmes and applying to this total a 'general allowance for shortfall' - amounting to £300 million - which is the Treasury's estimate of the net shortfall which is not reflected in departmental returns.

2. By its nature this £300 million cannot be allocated precisely to programmes in the White Paper, nor in the derived analyses by economic category, spending authority and department. For this reason it can be misleading to compare 1983-84 figures in this sort of detail with plans published in the previous White Paper or in the Autumn Statement. Nevertheless, the economic forecast suggests that the shortfall is mainly on local authorities current expenditure (about £100 million) and nationalised industries EFLs (about £200 million). Furthermore, an analysis of the current/capital split suggests that the White Paper figures for total current expenditure are reasonably accurate with most of the shortfall expected to fall on total capital expenditure.

3. The estimated outturn of £120.3 billion in the White Paper does not represent a change in view since the Autumn Statement - as the table below illustrates:

	£ billion
Total expenditure in national accounts terms - Autumn Statement Table 1.7	139
Change since FSBR	+ 1½
of which: on debt interest	+ ½
: directly affects planning total	+ 1
Planning total estimated outturn - FSBR Table 5.6	119.3
∴ Implicit estimated outturn underlying Autumn Statement	120.3

BACKGROUND NOTE: HOUSING BENEFIT CUTS

On Monday 6 February the Secretary of State for Social Services announced a number of modifications to the cuts in housing benefit announced in the Autumn Statement. The modifications took account of criticisms made by the Social Security Advisory Committee in a report which the Secretary of State published, along with the Government's response, on 6 February.

2. Original Proposals

The main features were:-

- (i) a sharp increase, from 21% to 31%, in the taper for assistance with rent (ie the rate at which households above the housing needs allowance lose benefit on income rises);
- (ii) an increase in the taper for assistance with rates from 7% to 9%;
- (iii) an increase in the level of minimum payments from 10p to £1 for rent assistance and from 20p to 50p for rate assistance (eliminating a large number of small claims, mainly to ease administration);
- (iv) an increase in the contributions expected from young working^{non}/dependents: 16-17 year olds to start contributing at a rate of £3.10 a week; contributions for 18-20 year olds to rise from £5.55 to £8.20; contributions from over 20s to rise from £6.55 to £8.20. (Note: Average weekly wages for 16-17 year olds are £61 (male), £55.70 (female), and for 18-20 year olds £95 (male), £78.20 (female);
- (v) to restrict the number of authorities which can give extra help to claimants in high rent areas. Qualifying threshold to be raised to 130% of national average rent.

3. The cumulative effects of the changes, in certain circumstances meant that some households (particularly those with young working^{non}/dependents) stood to lose significant amounts of money (extreme figures of £14 a week were quoted) and a number of occupational pensioners stood to lose over £3 a week. The local authorities also claimed it was impossible to implement the more complex changes from the proposed date of 1 April (for example, they have no records of the work

status of 16-17 year olds).

4. Modifications Announced

The main modifications announced on 6 February were:

- (i) the rent taper to rise to just 26% in April and 29% in November;
- (ii) the minimum payments to remain at their present level for those with incomes below the needs allowance;
- (iii) for those above the needs allowances, the minimum payments to rise to only 50p for rent and 50p for rates, and the changes to be postponed until November;
- (iv) the changes affecting 16-17 year olds to be postponed until November;
- (v) the changes to the high rent scheme also to be postponed until November.

5. The net effect of these concessions is that:-

- (i) the immediate impact of the cuts is softened for 1,300,000 families;
- (ii) 300,000 families who would have lost all benefit in April will not now do so (though some of them may lose entitlement in November);
- (iii) those with incomes below the needs allowance will now be unaffected by the changes in the tapers and minimum payments (though they may be affected immediately or in due course by some of the other changes);
- (iv) Average weekly losses will now be about 70p (59p for pensioners) in April and 88p (73p for pensioners) in November, compared with 96p (80p for pensioners) from April as originally proposed;
- (v) in April, 87% of pensioners and 81% of all claimants will lose less than £1 a week. For more than half of all claimants, losses will be less than 50p.
- (vi) local authorities' administration problems have been eased.

6. Mr Fowler has quoted the value of the concessions at about £45 million in 1984-85 and £15 million in later years. To help pay for this, he announced that the proposed real increase in the childrens needs allowance will be postponed. It was to have increased from £11.90 to £12.90 in April. It will now rise by 50p in November. But, Mr Fowler announced that there will be a further £1 rise in April 1985; so overall, there will be a real increase of £1.50 by April 1985 instead of the planned £1.

7. Public Expenditure Consequences

The original proposals were expected to yield savings of £230 million, of which £180 million was public expenditure. (Help with rates does not score on public expenditure). The revised package is expected to yield savings of £197 million in 1984-85 (£149 million of public expenditure) and £225 million (£175 million of public expenditure) in 1985-86. A small part of the difference (£8 million in 1984-85 and £3 million in 1985-86) will be met from the reserve. The remainder will be met by offsetting savings within the social security programme. (Note: for public consumption, Mr Fowler may quote the revised value of the savings as £185 million in 1984-85 and £230 million in 1985-86. That ignores the changes to the child needs allowance.

8. Because of printing schedules, the figures in the White Paper will be consistent with the original package.

9. Effect on the Poverty and Unemployment Trap.

The changes will mainly affect people whose incomes are too high to qualify for FIS and who are therefore above the worst part of the poverty trap. The changes will raise marginal rates for some, including about [130,000] working families, from 67% to 74% in April and 77% from November. For other families, including [150,000] working families, who lose entitlement to benefit altogether, marginal rates will fall from 67% to 39%.

10. The changes will worsen the unemployment trap, but the effect will not be dramatic. It is estimated that the proportion of the unemployed with ratios over 80% will rise from 21% to 22%.

11. The most considered outside reaction to the original proposals came from the Institute of Fiscal Studies (IFS). The modifications announced on 6 February would not significantly affect their conclusions which broadly endorse the line above.

12. Review of the housing benefit scheme

Mr Fowler announced on 6 February that he was setting up a review of the Housing Benefit scheme and its operation, under independent chairmanship to report to him. The objective will be "examine the structure and scope of the scheme to ensure it is as simple as possible and that help is concentrated on those most in need, and to improve its administration by local authorities".

BACKGROUND NOTE:LOCAL AUTHORITY CREDITWORTHINESS

1. Traditionally, local authorities have enjoyed a very high credit standing with the market. This is based on the legal requirement for an authority to make provision in its budget for servicing debt and then to rate to cover the budget; on the financial prudence imposed on an authority by not being allowed to borrow long-term for revenue purposes; on all debt having equal priority as a charge on the revenues of an authority; on the requirement for audit, the availability of the PWLB as a lender of last resort and the power of a lender to appoint a receiver.

2. During the passage of the Local Government Finance Act 1982, banning supplementary rates, we looked hard at the possible effect on creditworthiness and after some debate included a provision that "debt" as a charge on the revenues was to be taken to refer to both principle and interest. This was intended to be purely clarificatory, not to amend in any substantive way a situation which we believed to be quite adequate, and it appeared to satisfy the market for the time.

3. An article in the Financial Times on 31 January reported that concern was growing in the City that the Rates Bill would affect local authorities' creditworthiness because in English law lenders do not have an explicit first call on an authorities assets.

4. We are confident that neither rate limitation nor abolition will affects the real ability of authorities to service debt. Debt is specified to be "a charge" on the revenues of an authority; since it is the only such charge in law, lawyers advise that it is in practice the first charge. (In Scottish law the fact that it is the first charge is specific.) It is inconceivable that any authority should be affected by the new policies that it does not have the funds to service its debt if it gives that servicing the absolute priority laid down in law.

5. There is no Government guarantee of local authority borrowing. This does not matter legally for the above reason; neither does it seem to affect the market's view of creditworthiness much. The market does value the PWLB's lender of last resort facility, which provides a semblance of guarantee (although there is no absolute promise, in fact, that the Board will lend). The very existence of the facility has undoubtedly helped to make its use unnecessary! There is no question of any change in the PWLB rules.

6. We have been having discussions with CIFA (Mr Hepworth) and the Sterling Brokers' Association (Mr Packshaw), referred to in the FT article. We believe that neither body disputes the above interpretation of the actual legal position, but they think positive steps are needed to reassure the market. The Sterling Brokers seek a further cosmetic change to legislation going beyond that made in 1982. CIPFA are suggesting substantive legal changes to the budgeting and rate-setting duties of an authority and to the role of a treasurer vis-a-vis his councillors. We are not at present persuaded that any of the changes proposed are other than harmful. Discussions are continuing.

LINE TO TAKE

EFFECT OF RATE CAPPING

7. Will the Government set rate limits which will force local authorities to default on their loans?

[FT article, 31 January, reported concern that Rates Bill would impair local authorities creditworthiness.]

Concern about creditworthiness is utterly unfounded. It is true that English legislation does not describe lending as a first charge on an authority's revenues in so many words. But it is specified as being a charge - and since it is the only liability so specified anywhere in the whole of English legislation on local government, the charge is in effect a first charge. Secondly, there will be no change in the PWLB rules. I say with complete confidence that it is inconceivable that an authority would be so tightly constrained by rate limitation that it was unable to fulfil legal liability to lenders provided it gave them the absolute priority required by law.

8. If the general scheme is brought in could the Government not find it has accidentally set a rate limit that will force authorities into default?

If authorities think they cannot live within the rate ceiling they will have a chance to make representations to that effect before the limit becomes binding. But this is a matter for my Rt Hon Friend the Secretary of State for the Environment, and not of immediate relevance to the matter in hand.

9. What happens if an authority refuses to cut its expenditure to a level consistent with the rate ceiling and puts itself in a position where it cannot meet its debts?

Arrangements will clearly have to be made to deal with such a situation, but a decision on

what is the best approach remains to be taken. But this is primarily a matter for my Rt Hon Friend the Secretary of State for the Environment and not of immediate relevance to the matter in hand.

10. Will the Government have powers to appoint Commissioners if an authority puts itself in a position where it cannot pay the debts?

That is obviously one of the options we will have to consider, though there may be an alternative better solution. But this is a matter for my Rt Hon Friend the Secretary of State for the Environment and not relevant to the matter in hand. I hope authorities will act responsibly and that the situation will not arise.

ABOLITION OF THE GLC/MET COUNTY COUNCIL

11. Won't abolition prejudice the creditworthiness of the GLC/MCCs?

No. After abolition the existing debt of each authority will continue to be managed by a single body with all the necessary expertise. The debt will be funded by all the successor bodies; it will therefore continue to be backed by the rateable resources of the whole area.

BACKGROUND NOTE: ECGD'S NOTIONAL CASH BALANCES

Recent press comment related to ECGD's heavy claims experience and the running-out of its cash reserves may lead to interest in the public expenditure provision for ECGD.

This provision covers four specific programmes: interest support, refinance, cost escalation cover and the mixed credit matching facility.

Explanation

2. ECGD's credit insurance trading activities are intended to be self-financing and are not classified as public expenditure: a trading surplus or deficit on these activities is classified as revenue rather than expenditure, and is recorded in the Department's Trading Accounts.
3. ECGD's notional cash reserves from its trading operations, invested in the Consolidated Fund, are expected to be exhausted by the end of March 1984. It has been agreed that the Department may make borrowings from the Consolidated Fund, with an appropriate notional rate of interest being a charge in its Trading Accounts.
4. Although ECGD's net cash flow (excluding any notional items) increases or decreases the PSBR pound for pound, as long as the Department is able to service its notional loan from the Consolidated Fund, its trading activities will not be counted as public expenditure.