



10 DOWNING STREET

Prime Minister

Any comments? (I suggest
some censorship on page 10,
but this is very minor.)

I would delay your
approval until after
you have seen Tony
Thurston on Sunday
morning.

DRN

1/11

Excellent news. An
mark from the
US and President's name
no

cc BB
BC
14

FROM: CHIEF SECRETARY

DATE: 1 November 1985

PRIME MINISTER

PUBLIC EXPENDITURE CABINET

The Lord President is submitting to you a draft of the report of the MISC 120 Group. Agreement has now been reached on all programmes except housing. This minute sets out the arithmetic at the end of the Survey process and suggests how the remaining gap can be bridged and the way in which the results of the Survey should be presented.

The results of MISC 120

2. At its July meeting Cabinet decided that the planning totals should be

<u>£ billion</u>		
139.1	143.9	148.2

At the conclusion of the bilaterals, bids outstanding were some

3.4	4.7	5.7
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after allowing for lower reserves and higher asset sales proposed in July. As you are aware, I reconsidered the position on asset sales and the Reserve following the Cabinet meeting in October. In order to assist the Group in its work I concluded it was possible to reduce the Reserve and increase asset sales slightly more. I also considered a small addition of £0.5 billion could be made to the so far unpublished planning total in 1988-89.

3. During the course of the discussions on local authority current expenditure it became clear that agreement could be reached on the figures for 1987-88 and 1988-89 only by a very substantial addition to programmes, especially for education and law and order; or by setting the figures at the cash level for 1986-87 and transferring the increase that had previously been set aside (including the provision for restructuring of teachers' pay) to the Reserve. It was agreed to adopt the latter course and add £¼ billion, £¾ billion and £1 billion to the Reserve.

4. The net result of these changes is that the baseline against which the MISC 120 Report is measured embodies

	<u>£ billion</u>		
Planning total	139.1	143.9	148.7
Reserves	4.75	6.5	8.0
Asset sales	4.50	4.25	4.0

5. Lord Whitelaw has now reached a settlement with Michael Heseltine for defence at baseline for all three years.

6. Discussions are still continuing with Kenneth Baker to see if a settlement can be reached at the MISC 120 offer of

+120 +100 +80

7. I am still discussing with Peter Walker the figures for coal and gas but I expect these to be resolved at the figures I have proposed.

8. On Scotland, the Group has concluded that the option of a major revision of the block should not be pursued this year, though a study should now be set in hand. This leaves a number of smaller proposals to be sorted out. I hope to settle these with George Younger as soon as possible after he returns on Monday.

Closing the Gap

9. Table A attached sets out the position in relation to baseline which MISC 120 will be reporting to Cabinet at the conclusion of its work. Although, given the magnitude of the task, it has done well and driven some hard bargains there are overshoots of

0.2 0.25 0.1

Thus it will be clear to Cabinet that even if housing is settled at the Group's offer, which is incorporated into the figuring, our targets, revised in the third year, cannot be hit without some further adjustments by the Treasury. Obviously our first priority must be to settle housing, either before or at Cabinet, with the smallest possible addition to the offer. I believe there are good arguments for the position the Group has taken.

10. There is, however, a further element to be taken into account. The discussions on social security were conducted in the knowledge that revised costings were being prepared to take account of increases in the take-up of benefits. Our best estimates of the additions that are necessary over and above the MISC 120 figures are

+0.3 +0.3 +0.3

In addition, you advised that it would be better to revert to a flat profile for the assumption on unemployment. The effect of this is to add back

The Treasury had not brought your proposal of a fall between this year and next and flat thereafter. They are happy about it.

- +0.1 +0.2

I do not believe it is sensible to ignore these estimating changes; to do so would merely create a claim on the Reserve before the planning period has even begun. We should not plan on this basis especially when there are so many other potential claims on the Reserve.

SECRET

11. Adding in these estimating changes, the gap which I will have to bridge therefore becomes

0.5 0.65 0.6

plus any further concession which may be made on housing. I need, therefore, to be ready to cope with gaps of the order of

$\frac{1}{2}$ $\frac{3}{4}$ $\frac{3}{4}$

12. I start from the principle that it is extremely undesirable to make further additions to the published planning totals for years 1 and 2 which have already been increased in the Budget. This would undermine the principle of sticking to cash plans and undermine our ability to resist upward pressures in future Surveys. Some marginal adjustment could be made to the so far unpublished year 3 while remaining consistent to our objective of holding expenditure broadly constant in real terms and of securing a fall in the ratio of public expenditure to GDP.

13. The Reserves embodied in the MISC 120 arithmetic are substantial, but so too are the likely pressures upon them. We must, for example, be ready to meet the inevitable additions to local authority current expenditure for which no increase has been provided; and the settlement reached on social security in the last year is a provisional one, pending the outcome of the MISC 111 discussions. If we are to maintain Reserves which are both substantial and rising, there is only limited scope for further reductions.

14. On asset sales, however, the Chancellor and I believe a significant adjustment can be made. It is Government policy to achieve a very substantial transfer of assets to the private sector and we are progressively raising our sights in this area. Kenneth Baker will, for example, be bringing proposals to E(A) shortly recommending that regional water authorities be privatised. We could therefore publish more ambitious plans.

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The Chancellor and I can elaborate on our latest projections. We believe we should set ourselves the objective of sales of £4¾ billion in each year. This provides extra receipts of

*This looks well feasible
- see extra pps attached.*

<u>£ billion</u>		
$\frac{1}{4}$	$\frac{1}{2}$	$\frac{3}{4}$

15. There are difficulties to this course. We will have to counter the criticism that higher asset sales are being used to finance higher programmes. And if one of the major sales runs into difficulties we cannot at short notice put something in its place. In my view, this is another reason for ensuring that we have substantial Reserves so that the planning totals are not put under pressure in later years. Taking these risks into account, together with the other likely pressures, I believe we could adopt Reserves of:

<u>£ billion</u>		
$4\frac{1}{2}$	$6\frac{1}{4}$	8

16. This would contribute an extra

$\frac{1}{4}$	$\frac{1}{4}$	-
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and taken together with the increase in asset sales allow us to bridge the likely gap.

17. The figures we would present would then be

*You will want to ask
(a) what the last published figures were (I cannot say for sure)
(b) what the markets expect.*

	<u>£ billion</u>		
Planning total	139.1	143.9	148.7
Asset sales	4.75	4.75	4.75
Reserves	4.50	6.25	8.0

Next Steps

Scheduled for Monday morning 18. I would welcome the opportunity to discuss these proposals with you and the Chancellor. When we have agreed our approach (which may need minor adjustments to reflect any last minute changes in the arithmetic) I would not propose to circulate a paper to Cabinet. Assuming we reach a settlement on housing at the end of the Cabinet discussion, I or the Chancellor would

set out for colleagues broadly how we proposed to present the figures in the Autumn Statement. We could also offer to write to colleagues the following day setting out the figures precisely.



for JOHN MacGREGOR

[Approved by the Chief Secretary]

SECRET

TABLE A

MISC 120 PROPOSALS

	1986-87		1987-88		1988-89	
	Baseline	MISC 120 PROPOSALS	Baseline	MISC 120 PROPOSALS	Baseline	MISC 120 PROPOSALS
+ MOD(1)	18,560	0	18,859	0	19,033	0
+ FCO-ODA/ATP	1,296	21	1,317	29	1,350	37
+ ATP contributions + from other depts		-4		-11		-11
+ ENERGY	294	22	293	32	300	35
+ DOE-HOUSING	2,424	120	2,526	100	2,589	80
+ DOE-OTHER	848	-20	860	-20	882	-15
+ DES	3,418	81	3,505	75	3,593	60
+ OAL	333	7	342	9	350	12
+ HEALTH & PSS	14,945	250	15,622	300	16,012	600
+ SOCIAL SEC.	41,547	891	43,553	181	44,642	380
+ SCOTLAND	4,300	-27	4,373	-1	4,482	-18
+ Territorial + consequences		90		110		185
+ NAT IND						
+ Electricity	-1,447	31	-1,487	-198	-1,524	243
+ Water E&W	123	0	15	0	15	0
+ Coal	382	318	392	158	402	-2
+ BGC	-470	50				
+ TOTAL AGREED + IN BILATERALS	52,509	-1,675	53,724	-533	56,574	-1543
= PLANNING TOTALS	139,062	155	143,894	231	148,700	43

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TABLE B

PROGRAMMES AGREED OUTSIDE MISC 120P
1.11.85

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SCORECARD

£million

EX		1986-87		1987-88		1988-89	
		Baseline 999,999	AGREED 99,999	Baseline 999,999	AGREED 99999	Baseline 999,999	AGREED 99999
+	1. FCO-OTHER	603	38	619	43	635	63
+	2. EC	640	10	830	320	850	100
+	3. IBAP/AFF CAP	1,277	272	1,304	334	1,337	336
+	4. AFF domestic	713	8	699	5	717	3
+	5. FORESTRY	53	0	54	0	56	0
+	6. TRADE/INDUSTR	1,162	-13	980	12	1,004	-25
+	7. ECGD	78	200	-43	213	-44	138
+	8. EMPLOYMENT	3,704	-74	3,901	-207	3,999	-125
+	9. TRANSPORT	1,955	27	1,995	33	2,045	52
+	10. DOE-PSA	-120	7	-128	0	-131	0
+	11. LCD	574	21	610	39	625	73
+	12. HOME OFFICE	1,061	43	1,104	44	1,131	55
+	13. CIVIL SUPER	1,114	65	1,226	86	1,257	147
+	14. WALES	1,708	-1	1,735	-1	1,779	-4
+	15. N. IRELAND	4,464	53	4,603	76	4,717	105
+	16. CHANCELLOR'S	1,825	163	1,842	169	1,888	143
+	17. OTHER (inc ter consequences)	366	170	396	170	406	205
	NAT IND						
+	20. Settled	1,495	-4	1,265	-77	1,299	-459
+	21. RMPS & SRP	309	194	318	-41	326	-50
+	23. BGC			-390	390	-400	400
+	24. LA REL CUR(UKA)	26,032	646	26,301	359	26,959	-323
+	25. SPECIAL SALES OF ASSETS	-2,250	-2,250	-2,250	-2000	-2,250	-1750
+	26. RESERVE	6,000	-1,250	7,000	-500	7,000	1000
+	27. 3.3 % increase in 1988-89					1,627	-1627
+	28. less double counting	-254		-247		-258	
+=	TOTAL AGREED	52,509	-1,675	53,724	-533	56,574	-1543

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CLON POL : Public Expend R 33

