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SECRET

Prime Minister 2

Fair point.

David Norgrove Esq
Private Secretary
10 Downing Street
London SW1

DCW 5/11

5 November 1986

Dear David

AUTUMN STATEMENT PUBLICITY

At the conclusion of yesterday's meeting between MISC 130 and my Secretary of State it was agreed that it would be for him to consider how the settlement then reached might be presented (page 3 of MISC 130(86) 25th meeting refers).

Mr Rifkind will be considering the presentational aspects in the course of deciding on allocations within the provision for his programmes with a view to making an announcement about the middle of December. In order to maintain the room for manoeuvre which MISC 130 agreed that he should have, he would be glad if there was no mention of specific aspects of the discussions in MISC 130 such as adjustments to reflect changes in population ratios since 1979 for either the Scotland or Wales programmes in any general briefing which may be released to accompany the Autumn Statement.

I am copying this letter to Alex Allan and Colin Williams.

Yours ever

Robert Gordon

ROBERT GORDON
Private Secretary

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cc MAA BI
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Prime Minister
The latest ver

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With permission, Mr Speaker, I should like to make a statement.

Cabinet today agreed the Government's public expenditure plans for the next three years.

In the normal course of events that would be followed by the publication of the printed Autumn Statement, accompanied by an Oral Statement to the House, next Tuesday.

For obvious reasons that is not possible this year.

So while the Autumn Statement will be printed in the normal way and presented to Parliament as soon as the House reassembles next Wednesday, I thought it would be for the convenience of the House if I made my Oral Statement today.

This will cover all three of the key elements in the printed Statement: the Government's outline public expenditure plans for each of the next three years and the expected outturn for this year; proposals for next year's national insurance contributions; and the forecast of the economic prospects for 1987 required by the 1975 Industry Act.

The full text of the economic forecast, together with the public expenditure figures and the rest of the information customarily published with this Statement will be available from the Vote Office as soon as I have sat down.

They will also appear in the printed Autumn Statement to be published next week.

I turn first to the outturn for the current financial year, 1986-87.

The public expenditure planning total now looks likely to amount to almost £140½ billion - £1¼ billion, or a little less than 1 per cent, above what was allowed for in this year's Public Expenditure White Paper.

The main reason for this excess is a 9 per cent rise in the current spending of local authorities - far more than was provided for.

However, other items on the expenditure side, the largest of which is debt interest, are likely to fall short of what was forecast at the time of the Budget, thus reducing the total overrun on the expenditure side to about £½ billion.

On the receipts side, the North Sea tax take is likely to be even lower, by about £1 billion, than I envisaged at the time of the Budget, largely because for a long period the oil price has been below the $15 a barrel level on which the Budget arithmetic was explicitly based.

This shortfall, however, is more than offset by the continuing buoyancy of non-oil tax revenues, in particular VAT and Corporation Tax.

Non-oil revenues now look likely to exceed the Budget forecast by £2 billion.

This would imply a net overrun on the receipts side of about £1 billion, rather more than that on the expenditure side.

But this will be reduced by a change I propose to make to the North Sea fiscal regime.

The collapse of the oil price has led to a sharp cutback in investment activity in the North Sea, with inevitable consequences for the UK offshore supplies industry both in Scotland and the North East of England.

Against this background the Government is conducting a review of the North Sea fiscal regime, and I shall be announcing my conclusions in the Budget in the light of that review.

But given the current difficulties of the offshore supplies industry, there is one change I believe it right to make without further delay.

I propose, on a carefully targeted basis, to accelerate the arrangements for the repayment to the oil companies of Advance Petroleum Revenue Tax due to them.

The details of this change, which will require legislation early in the new Session of Parliament, are set out in a Press Notice which the Inland Revenue will be issuing as soon as I have sat down.

The new arrangements will have a revenue cost this financial year of some £300m, which will be fully recouped over the next three years.

Taking this into account, the Public Sector Borrowing Requirement for the current year is still forecast to be about £7 billion, the figure I set in the Budget.

I turn now to the public expenditure plans for the next three years.

This year, for the fourth successive year, public spending, both before and after deducting the proceeds of privatisation, is set to decline as a proportion of national output.

The Government is determined to ensure that this trend continues: to see to it that total public spending, even without taking account of privatisation proceeds, continues to decline as a percentage of GDP.

The plans I am about to announce for the next three years secure that objective.

Indeed, they show that by the end of the period the ratio of public spending to national output will be back to the level of the early seventies.

But within this overall constraint, and in the context of its policy priorities, the Government has felt it right to allow an increase in the previously announced planning totals for 1987-88 and 1988-89.

Compared with the prospective outturn for the current year, we are now planning for an average growth in the public expenditure planning total of about 1¼ per cent a year in real terms, well within the prospective growth of the economy as a whole.

The new planning totals have thus been set at £148½ billion for 1987-88 and £154½ billion in 1988-89, an increase of £4¾ billion and £5½ billion respectively.

For 1989-90 the planning total has been set at £161½ billion.

As usual, these totals incorporate estimates for the proceeds of privatisation.

Last year I increased the estimate of these proceeds very substantially to £4¾ billion in each of the three Survey years, a figure which I expect to be duly achieved this year.

Although the privatisation programme is now moving ahead more strongly than ever before, I have decided to make only a modest further addition to this estimate, bringing it to £5 billion in each of the next three years.

The new planning totals also contain substantial reserves, rising from £3½billion in 1987-88 to £7½ billion in 1989-90.

The public expenditure increases I have announced allow us to make realistic provision both for local authority current expenditure, over which the Government has no direct control, and for demand-led programmes such as social security, while still leaving scope for increased spending on services to which the Government attaches particular priority.

But before referring to some of the more important changes, let me make one thing absolutely clear.

There can be no question of allowing the projected increases in public expenditure over the next two years to undermine the prudence of the Government's overall fiscal stance.

The Government's fiscal stance has been clearly set out in the medium-term financial strategy published at the time of this year's Budget.

There will be no relaxation of that stance.

Within the totality of public expenditure, the largest increase is for the local authorities, whose current spending next year is now put at £4 billion above the previous provision.

This in part reflects the fact that the previous plans simply carried forward the same level of cash spending as in 1986-87.

At the same time, we are increasing next year's Aggregate Exchequer Grant - the contribution that taxpayers make to local government spending - by almost 10 per cent over this year's Settlement; a rise of almost £1½ billion.

These substantial sums demonstrate in particular the priority the Government is giving to education, which, including the new proposals on pay and conditions of service for teachers announced last week, accounts for about half the increase in provision.

A further major portion of the increase is for the police.

On top of the increased provision for the cost of education in schools, which is contained within local authority current spending, there will be additional provision for the universities of £60 million in 1987-88 and £70 million in 1988-89.

Spending on the health and personal social services will be increased by more than £600 million.

For the National Health Service alone, the increase in England amounts to over £300 million a year.

Combined with the additional resources being generated by greater efficiency, this will not only enable the Health Service to cope with the growing number of elderly patients but will also allow it to improve services.

Gross provision for housing investment is being increased by £450 million.

This will sustain the rising trend of spending on local authority renovation and improvements and provide additional resources for the housing associations.

In the light of this year's experience, £1¾ billion has been added to next year's provision for social security, most of which represents a greater expected expenditure on existing means-tested benefits.

Provision for investment in roads is being increased by £65 million next year and £75 million the year after, mostly for local authority roads.

For defence, the provision remains as planned in the last White Paper after allowing for minor changes, including a reduction in the estimated cost of the Falklands deployment.

The defence programme will continue to benefit from the substantial real growth in previous years and the wide-ranging action to improve efficiency and value for money.

Taking all programmes together, the additions to planned capital expenditure amount to getting on for £1 billion in 1987-88, of which about two-thirds is local authority spending.

Further details of these and other changes will be contained in the printed Autumn Statement which will be published as soon as the House returns next week.

In addition, full details, together with information on running costs and manpower, will be given in the public expenditure White Paper early in the New Year.

I now turn to National Insurance contributions.

The Government have conducted the usual Autumn review of contributions in the light of advice from the Government Actuary on the prospective income and expenditure of the national insurance fund, and taking account of the benefit uprating which my Rt Hon Friend the Secretary of State for Social Services announced on 22 October.

The lower earnings limit will be increased next April to £39 a week, in line with the single person's pension, and the upper earnings limit will be similarly raised to £295 a week.

The limits for the reduced rate bands which I announced in last year's Budget will also be increased again in April, but by proportionately larger amounts.

The upper limit for the 5 per cent and 7 per cent bands will be raised to £65 a week and £100 a week respectively, and the upper limit for the 9 per cent rate for employers will be raised to £150 a week.

The taxpayer's contribution to the National Insurance Fund - the so-called Treasury Supplement - will be reduced by 2 per cent to 7 per cent, but this will not require any change in contribution rates.

Thus the main Class I contribution rates will once again remain unchanged at 9 per cent for employees and 10.45 per cent for employers.

Finally, I turn to the Industry Act Forecast.

Both growth and inflation have turned out to be slightly lower this year than I envisaged at the time of the Budget.

Growth now looks like turning out at 2½ per cent, against a Budget forecast of 3 per cent, and inflation in the fourth quarter of this year is likely to be 3¾ per cent, against the Budget forecast of 3½ per cent.

The principal reason for this slower growth has been the disappointing performance of exports, which were hard hit by the cutback in spending by OPEC and other primary producers affected by the sharp fall in commodity prices in general and the oil price in particular.

Combined with a halving in the value of our own oil exports, this has meant a significant deterioration in the current account of the balance of payments, from a surplus of some £3½ billion in 1985 - and a cumulative surplus of £21 billion over the six years from 1980 to 1985 inclusive -to a forecast of broad balance for 1986.

Looking ahead to 1987 the prospects are generally encouraging.

While the necessary adjustment of the exchange rate to the oil price collapse has now taken place, it will inevitably take time before the full benefits come through in higher non-oil exports and reduced import penetration at home.

This means we can expect the current account of the balance of payments to go into deficit next year, for the first time since 1979, to the tune of some £1½ billion.

Even so, non-oil exports are forecast to rise next year by 5½ per cent, compared with an increase of only 1 per cent this year, with manufacturing output, in consequence, up by 4 per cent.

And with domestic demand continuing to expand at the same rate as this year, the economy overall is likely to grow by a further 3 per cent next year - the sixth successive year of steady growth at an average annual rate of almost 3 per cent.

Recorded inflation is likely to edge up a little, to 3¾ per cent in the Fourth Quarter of 1987.

This is almost entirely due to the effect on the RPI of the timing of mortgage rate changes.

The Government's commitment to a monetary policy that will squeeze out inflation remains unabated.

Meanwhile the likelihood of faster growth next year, coming at a time when unemployment already appears to have stopped rising, suggests that the prospects for some fall in unemployment are now more promising.

But this promise could still be frustrated by excessive pay settlements.

Mr Speaker, the strategy we have followed since 1979 has brought inflation down to the lowest level for two decades, combined with sustained growth and steadily rising living standards.

This is a combination that has eluded successive Governments for a generation.

We have brought it about by the determined pursuit of free markets and sound money.

And that is what we will stick to.