PRIME MINISTER PUBLIC SPENDING I think I should tell you - and David Norgrove agrees - that I am very apprehensive about the presentation of the expected decision on the public expenditure review at Cabinet tomorrow. This will be the first time that we have not publicly, at this the July Cabinet stage in the PES round, reaffirmed the objective of keeping within the planning totals. This will come to the media as a significant departure, with serious implications for confidence and continued Government resolve to control public expenditure. The situation is potentially all the more serious because the media quite deliberately, for reasons internal to Government,

have not been prepared for it.

The more I have prepared for the presentation, the more concerned I have become and that concern is reflected in the sort of media questions I might expect which are set out at Annex I.

These questions and the proposed statement at Annex II formed the basis for a discussion with Treasury yesterday.

On my advice they are considering whether I can be authorised to say - as I feel I must be - something to this effect:

"The Cabinet has made no change to the planning total agreed on the need to keep as close to them as possible as well as achieving the overriding objective that public worlditure should take a steadily smaller share of our "The Cabinet has made no change to the planning totals. It national income." this is weak - mit.

> It is difficult to say whether this will do the trick. But I am absolutely clear in my mind that without my being able to say that we are in very dangerous territory indeed.

The Treasury are drafting Answers to the key questions in Annex I on the basis that appropriate reference is made to the planning totals.

BERNARD INGHAM 22 July 1987

1.

QUESTIONS

- 1. The Manifesto said: "Our aim is to ensure that public expenditure takes a steadily smaller share of our national income". Your statement today reaffirms that policy. It makes no mention of planning totals. Are you still seeking to achieve those planning totals £154.2bn (1988-89); £161.5bn (1989-90)?
- 2. Is this not the first time you have not specifically set as the objective for the autumn round the containment of spending within those totals?
- 3. Does the failure this time to use those planning totals as the basis for the autumnal operation mean that you have abandoned them at the outset of the exercise?
- 4. If so, why have you abandoned them? Is it because they were set unrealistically low? Or that next year's contingency is unrealistically tight already? Or that you feel that the purse strings can be loosened a bit as we enter the seventh successive year of economic growth?
- 5. If the last, how do you propose to continue to curb the appetite of wage negotiators?
- 6. How much are bids over the top? Where are the pressure points - Defence, Health, Social Security, Housing, Education, Local Government, Inner Cities?
- 7. If you are not to seek to adhere to planning totals, what levels of expenditure do you have in mind?
- 8. How are you to exercise discipline, and curb demands, if you don't have cash totals to aim for?
- 9. Isn't it a fact that since no one knows what national income will be in 1988-89 et seq you are swapping a corset for stretch trousers to accommodate elasticity?
- 10. Is it not a fact that the projected national income includes an allowance for inflation? If so, are you not automatically indexing expenditure before you start to curb demand, and thereby further weakening the control mechanism?
- 11. Will there be any need for a Star Chamber in view of this relaxation?

- 12. What effect will all this uncertainty about the future course of expenditure have on confidence? Isn't this the first major economic U-turn of the Prime Minister's Administration?
- 13. Are any moves to be made to try to tighten up on the efficiency with which Government spends money to try to sugar the pill?
- 14. What will happen if, as some commentators fear, the economy fails to grow, or fails to grow as rapidly as you forecast? Is the Government then prepared to raise taxes?
- 15. What, if any, are the prospects for tax cuts in the Spring in view of this manifest setback over spending?
- 16. Are we not beginning to see the first inklings of the trouble ahead which was forecast by the Opposition during the election - starting with spending out of control, overheating and rapidly deteriorating trade balance?
- 17. Alternatively, why should we remain optimistic about the future stewardship of the nation's finances and taxes over the coming years?
- 18. How do you characterise the bilaterals to come in September/October the toughest yet? Or what?