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Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon Norman Fowler MP
 Secretary of State for Employment
 Department of Employment
 Caxton House
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25th June 1988

Dear Norman,

1988 PUBLIC EXPENDITURE SURVEY: EMPLOYMENT

Thank you for your letter of 26 May, setting out your proposals for the 1988 Public Expenditure Survey.

Those proposals involve substantial additions to both programme and running costs, rising from £200 million in 1989-90. I find such large bids difficult to justify against the background of the markedly improved labour market we now see. Indeed I see a strong case for looking for reductions rather than increases.

The employment programme has expanded at a quite exceptional rate over the past 10 years - 78 per cent in real terms, compared with 13 per cent for the planning total - a rate unmatched by any other major programme. That reflects the high priority which we have given to tackling unemployment. Unemployment is now falling rapidly - by some 40,000 a month - largely due to the success of our economic policies. It is now back to levels last seen at the beginning of the decade - and then the employment programme was more than £900 million lower in today's prices than the level now planned.

I recognise that you have already begun to change the direction of your programme to take account of falling unemployment. But we also need to take a fairly fundamental look at the scale of the programme, and to ask our officials to establish urgently the needs to be met and the scope for

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reductions. We can then consider all the options in our bilateral discussions in due course.

We will of course not get significant savings without looking closely at the two largest programmes, Employment Training and the Youth Training Scheme. On the former, the inflow into the target groups is bound to be affected by the improving unemployment situation. The fall in long-term unemployment is particularly relevant: at more than 20 per cent over the past year, and fairly evenly spread across all regions except Ulster, it is now faster than for unemployment generally. The announced opposition of major unions is also likely to have some effect on take-up. There are moreover questions about the rate at which we need to aim to cover the stock of 18 - 50 year olds unemployed for over two years, and about the length of time for which participants remain in the programme. In the light of all these considerations I think that we will need to review the assumptions underlying the estimate of some 600,000 beneficiaries in the February White Paper.

It may be argued that we need more experience of the new scheme before we can modify the assumptions with any confidence. But I do not believe that the newness of the scheme reduces the need for taut estimating. The number that it needs to cover is bound to grow less as unemployment falls. How much less is something which we will have to decide, but I think that officials should now examine the effect of a range of assumptions.

YTS will be profoundly affected not just by the decline in unemployment, but also by the dramatic decline in the size of the relevant age group which is already taking place. Over the PES period, we can expect a marked tightening of the relevant labour market, to an extent which calls into serious question the need for Government intervention on a national basis. The opportunities currently offered by YTS will increasingly become available without Government subsidy. I do not overlook the important training aspect of YTS; but here again there is likely to be dead weight in subsidising training which employers would have had to do anyway. Against this background there is a strong case for selectivity, and for not treating all training (even for occupations in which the real skill content is very low) as if it were of equal value.

I therefore think that officials should explore options to reduce dead weight and the resulting unjustified element of subsidy to employers. It is after all our policy that employers should bear a fair share of the cost; and you have told the Commission that employers will have to increase the contribution they made to the cost of the YTS over the PES period. One initial step would be to pay no more than the trainee allowance outside inner cities and assisted areas (for similar geographical areas). That would reduce (though not eliminate) the subsidy to employers which is inherent in the scheme at present and is becoming increasingly difficult to justify. The new funding structure which is the subject of your letter of 27 May (which has reached me only last week and to which I will be replying separately) may also provide some flexibility for moderating the level of subsidy.

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I also think that officials need to look closely at the estimation of provision for YTS. Even allowing for the ending of income support for the relevant age group, the present provision looks as if it could be a good deal too high. There must be a strong probability that, as the labour market tightens, young people will go straight into paid employment rather than YTS, which may increasingly look a less attractive alternative to them.

Much of what I have said about the general case for reductions applies to other elements of your programme. There are a number of small schemes, notably Jobstart, which might be dropped altogether. Then there may well be a case for being more selective, perhaps on a regional basis, with both the Enterprise Allowance Scheme and the Business Improvement Initiative. On the former, savings might also be made (and value for money improved) by adopting some of the suggestions in the scrutiny report produced last autumn, such as tighter eligibility criteria. On the latter, the shift in funding from training to consultancy ought to mean a reduction in provision. Restart is another potential area for savings: the courses should no longer be needed now that we have ET. Then there is publicity, on which your Department's spending is very high as a proportion of the total programme. The need to secure higher visibility for your programmes must now be a good deal less than it was.

Outside the immediate field of employment and training measures, there appears to be further potential for savings. You have initiated a review of tourism policy. I think that we will need to consider very carefully whether any Government support is justified for an increasingly prosperous industry like tourism. An evaluation of the Small Firms Loan Guarantee Scheme is now drawing to a conclusion, and we will have to decide whether the scheme should be extended beyond next year. I think that we will need to consider very carefully whether such a scheme continues to be justified.

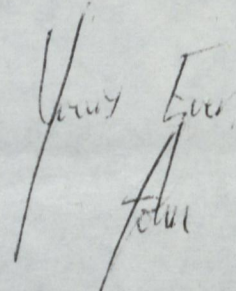
The major element of your running costs bid is for pay and prices. I would have hoped to see a greater contribution to offsetting this from efficiency savings. Another major element relates to the stricter benefit regime, the case for which is also argued in your letter of 6 June. I can see why you wish to give this some priority, but I think that more attention needs to be given to the scope for offsetting savings. In this connection the role of the Jobcentres seems to me to be an area worth examining. They have a role to play, but in the improving labour market I question whether it should include their employment agency function for job changers, which would be better carried out by the private sector. I hope that officials can identify options for us to consider here.

This letter has raised a wide range of questions about your programme. They are not questions on which I have yet taken a firm view myself, but I think that we are bound to address

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them in this Survey; and the main purpose of this letter is to ensure that the necessary preparatory work is done. We are faced with an increasingly radical shift in the employment situation to which your programmes are intended to respond. The priority which those programmes were given at a time of rising unemployment must imply a fairly major reassessment now.

I am copying this letter to the Prime Minister.

A handwritten signature in dark ink, appearing to read 'John Major', written in a cursive style.

JOHN MAJOR

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