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From the Private Secretary

26 June 1989

Dear Caryl,

1989 PUBLIC EXPENDITURE SURVEY

The Prime Minister was grateful for the Chief Secretary's minute of 23 June, and has noted the latest position on Ministers' bids.

She would be grateful if the Chief Secretary could let her have a further note later this week setting out specific proposals on the remit that Cabinet might be invited to endorse. She would like to discuss this with the Chancellor and the Chief Secretary early next week.

I am copying this letter to Alex Allan (HM Treasury).

Yan.
Paul

(PAUL GRAY)

Miss Carys Evans,
Chief Secretary's Office.

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cc Bagwell



FROM: CHIEF SECRETARY
DATE: 23 June 1989

PRIME MINISTER
1989 SURVEY

Prop Part 41

My minute of 12 May warned that we would face strong upward pressure on many spending programmes in the coming Survey. Colleagues have now sent me their bids for the three Survey years.

2. The bids are even higher than I had expected, totalling £13 billion in 1990-91, and £15 billion and £21 billion respectively in the two later years. A number of these bids represent very large percentage increases on the departmental baselines - for instance, nearly 25 per cent for DES in 1990-91, and even more for DTp. In addition to this several colleagues noted that there were further bids to come, and a number warned that they would need to reconsider their bids if the inflation assumptions were increased.

social security is bound to be ready

£16 billion hide because of the RPI. RPI 6

3. I have been through the bidding letters very carefully.

4. As we foresaw, there are a hard core of bids, amounting now to around £4 billion, which are virtually irresistible. These include the cost of policies to which we are already publicly committed, on student loans, for example, and on the pensioners earnings rule. They also include the effect of higher inflation on social security upratings; and the extra AEF for English local authorities, which E(LF) has just agreed, along with comparable increases for Scotland and Wales.

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5. There are other bids where some additional spending is probably inevitable, though the sums sought by colleagues will need to be pruned. For example, Kenneth Clarke's bid of £1½ billion in 1990-91 for the health service includes some £½ billion for the costs of implementing the NHS Review.

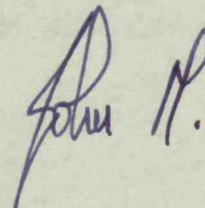
6. A particular group of bids is for extra capital investment in housing, education, prisons, roads, rail, and health; these already total over £3¼ billion in 1990-91; further bids are yet to come on rail, particularly for the later years. Individual bids may be well supported: for example Paul Channon's bid for greatly expanded road investment follows E(A)'s decision, and his recent White Paper. Taken together, however, they amount to a wholly unrealistic expansion of public sector investment. Quite apart from its cost, this would put a severe strain on the capacity of the supplying industries, with adverse effects on both prices and imports.

7. The overall bids are almost a third higher than they were at this stage last year. Further bids of about £3-4 billion a year emerged during the course of last year's Survey and something similar is likely to happen again. Last year, the eventual outcome was transformed by savings of nearly £5 billion a year which emerged on unemployment benefit, housing receipts, the nationalised industries and agricultural market support. These savings reflected the success of our policies, but have now already been built into the plans for the present Survey years. We cannot therefore expect a similar last-minute reprieve this time.

8. We clearly cannot contemplate increasing expenditure to anything like the extent sought by colleagues. It would be quite irresponsible in the present economic situation. It would put off indefinitely our hopes of reducing the present tax burden as a proportion of national income, still less of getting back to the level we inherited ten years ago.

9. I am also concerned about public expectations of the prospective scale of extra spending on the infrastructure. I shall be seeking to inject a greater sense of realism into this debate in a speech I shall be making to the Adam Smith Institute on 27 June.

10. This is bound to be a very tough Survey even by recent standards. I shall be writing straight away, on a personal basis, to a few selected colleagues including Paul Channon and Kenneth Baker, urging them to re-examine their priorities. I have also warned Norman Fowler that I shall once again need to seek very substantial cuts in the employment programme. But the bulk of the bilateral discussion will have to wait until after the Cabinet on 12 July. I hope colleagues will agree then that the present economic climate requires severe pruning of their initial bids if we are to retain the credibility of our medium term economic and fiscal aims.



JOHN MAJOR

ECON PA: Public Expenditure Part 42



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