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PRIME MINISTER

CABINET DISCUSSION ON PUBLIC EXPENDITURE

The papers are:

- Flag A - The Chancellor's paper on economic prospects (C(89)9).
- Flag B - The Chief Secretary's paper on public expenditure (C(89)8).
- Flag C - A speaking note for your use in opening the discussion, prepared by the Treasury.
- Flag D - Cabinet Office briefing. This includes (paragraph 14) the proposed form of words for Bernard to use in briefing the Press.
- Flag E - The further material the Chief Secretary circulated detailing all the additional bids Ministers have submitted (no need for you to go through this, but you may want to have it to hand for the discussion).

Two points on handling:

- (i) There would be advantage in completing the public expenditure discussion before 11 a.m., so that Bernard is in a position to brief the Lobby on the outcome.
- (ii) As usual, you will want to consider the best order in which to invite colleagues to speak. I assume you will want:
- after the Chancellor and Chief Secretary to have a number of supporters;
 - to sandwich the critical voices in between supporters;

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- to end with a strong supporter.

A possible order, bearing in mind that Mr. Younger is absent, would be:

Chancellor of the Exchequer
Chief Secretary
Secretary of State for the Environment
Secretary of State for Employment
Home Secretary
Secretary of State for Social Security
Lord President
Secretary of State for Education and Science
Minister of Agriculture, Fisheries and Food
Secretary of State for Northern Ireland
Secretary of State for Wales
Secretary of State for Trade and Industry
Secretary of State for Scotland
Secretary of State for Health
Lord Chancellor
Secretary of State for Energy
Chancellor of the Duchy of Lancaster
Secretary of State for Transport
Lord Privy Seal
Foreign Secretary

Derek [Signature]

Duty Clerk

+ PG

11 July, 1989.



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PRIME MINISTER

PUBLIC EXPENDITURE

Economic Prospects: C(89)9
Memorandum by the Chancellor of the Exchequer
1989 Public Expenditure Survey: C(89)8
Memorandum by the Chief Secretary, Treasury.

DECISIONS

No conclusions are needed on the Chancellor's paper, C(89)9. But you will want the Cabinet to endorse the conclusions in paragraph 15 of the Chief Secretary's paper, C(89)8. The most important of these concerns the Government's objective for the public expenditure figures. The Chief Secretary also proposes that, if necessary, a small group should be set up in October to consider outstanding issues when the bilaterals are concluded. Finally, you will want to agree what should be said to the Press after this Cabinet.

MAIN POINTS

Economic prospects

2. No decisions are needed on the Chancellor's paper on economic prospects and you may prefer to avoid an extensive discussion of the subject.

3. Ministers may note the following worrying features in the forecasts in the paper and annex:

i. The GDP deflator is forecast at 7% for 1989 over 1988, compared with 5½% in the Budget forecast.

ii. The current balance deficit is forecast at £16 bn for 1989, compared with £14½ bn in the budget forecast.



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4. The Chancellor is likely in his opening remarks to give the Cabinet the GDP deflator forecasts for later years. They are as follows:

	New forecasts	Previous forecasts
1990-91	5 %	4 %
1991-92	3½%	3 %
1992-93	3 %	2½%

The new forecasts may prompt some Ministers to press for adjustments to Departmental programmes to reflect higher inflation.

5. You may wish to draw the conclusion, as the Chancellor does, that the economic prospects demonstrate the need for a continuing prudent fiscal policy and restraint in public spending.

The objective for public expenditure

6. The Chief Secretary proposes the following objectives:

- i. maintain the downward trend in the ratio of public spending (excluding privatisation proceeds) to GDP. This reflects long-standing policy. A similar objective was agreed last year, and restated in the Financial Statement and Budget Report.
- ii. hold as close as possible to existing plans. This objective does not refer, as last year's did, to the planning total. This is because the planning total has been re-defined to exclude local authority expenditure financed by rates or the community charge.

7. There may be some speculation by Ministers about what increases in expenditure would be consistent with these



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objectives. You may wish to discourage any such speculation, and endorse the objectives.

8. The Chief Secretary is not planning this year to refer to individual programmes in his opening remarks. His paper says only that the total of bids is far in excess of what could be afforded consistent with the objectives. He does not however give a figure for this total since it would be damaging if leaked. You may prefer the discussion not to get into figures.

9. Other points on which you may wish to draw if necessary are:

i. need for restraint. At a time when private spending is being held back by the measures needed to reduce inflation, it is even more important to ensure continued tight control of public spending.

ii. cash planning. The Government should adhere to the presumption underlying cash planning that inflation is not automatically accommodated. The new figures to be given by the Chancellor for the GDP deflator for later years make this point more important.

iii. construction industry. It is important to take account of the pressures in the construction industry. Ambitious programmes involving more construction might lead to higher prices rather than more output.

Aggregate Exchequer Finance for local authorities

10. The Chief Secretary's paper reports the settlement on local authority finance reached by E(LF) under your Chairmanship (paragraph 10). There seems no need to discuss this. (The Treasury now say that the addition to the planning total, taking account of territorial repercussions, will be about £1½ bn rather



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than the £1 bn in the paper).

Running costs

11. The Chief Secretary does not this year recommend a specific objective on running costs, but proposes that spending on the Civil Service should be substantially lower than implied in running cost bids and that Ministers should look for more ambitious plans to contain costs and improve efficiency. You will wish to endorse these proposals and ask Ministers to give their personal attention to Departmental plans to contain costs and improve efficiency.

Nationalised industries

12. The Chief Secretary recommends aiming at substantial reductions in the additional bids from the nationalised industries. You will wish to endorse this.

Future discussions

13. The Chief Secretary recommends that he should now conduct bilaterals with his colleagues. They should be complete by early October. It is not yet clear whether a Star Chamber will then be needed but it would be useful to have formal agreement now that one can be set up if necessary, without the need for further discussion in October. You may however wish to avoid any reference to the chairmanship. You could say that you hoped that the Chief Secretary would be able to reach agreement with his colleagues on the basis proposed but that if this proved impossible you would at the appropriate time establish a small group to consider outstanding issues and to make recommendations to the Cabinet.

Handling the Press

14. The Press will ask about the outcome of the Cabinet. As usual you will wish to agree a form of words which your Press



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Office can use in briefing them after Cabinet. The Treasury have suggested the following which you could read out to Cabinet:

"The Cabinet had its usual July discussion of public expenditure today. It agreed that the objective should be to maintain the downward trend in the ratio of public spending (excluding privatisation proceeds) to GDP, and hold as close as possible to existing plans. With this objective, the Chief Secretary will hold bilateral discussions in the Autumn. In the light of these, the Government will take decisions on individual programmes and the planning totals, and these will be announced as usual, in the Autumn Statement in November."

You might also emphasise that other members of the Cabinet should adhere to this line, that bilaterals should be carried out in confidence, and that the media should be given no ground on which to base speculative stories of Ministerial disagreements.

HANDLING

15. You will wish to invite the Chancellor of the Exchequer to open the discussion by describing the current economic background and prospects and the Chief Secretary, Treasury to follow with a more detailed account of his proposals on public expenditure. All members of the Cabinet may wish to contribute to the subsequent discussion.

R.R.B.

ROBIN BUTLER
Cabinet Office
11 July 1989

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PM

PM

- 1. Chancellor of the Exchequer
- 2. Chief Secretary
- 12. ~~12.~~ Trade and Industry
- 4. Employment
- 9. Agriculture
- ~~Defence~~
- 7. Lord President
- 3. Environment
- 20. Foreign Secretary
- 13. Scotland
- 14. Health and Social Security
- 8. Education
- 5. Home Office
- 11. Wales
- 10. Northern Ireland
- 18. Transport
- 15. Lord Chancellor
- 16. Energy
- ~~Chief Secretary~~
- ~~Chancellor of the Exchequer~~

- Chancellor of the Exchequer
- Chief Secretary
- Defence
- Employment
- Environment
- Health and Social Security
- Chancellor of the Duchy
- Lord President
- Home Secretary
- Education
- Northern Ireland
- Scotland
- Wales
- Energy
- Foreign Secretary
- Transport
- Chief Secretary
- Chancellor of the Exchequer

~~19. *Antehead.*~~
 17. C.D.L.
 19. *B* LPS