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FROM: CHIEF SECRETARY
DATE: 24 October 1989

PRIME MINISTER

1989 PUBLIC EXPENDITURE SURVEY

I thought you would like to have a brief report on progress so far in the public expenditure round.

2 I have been able to reach substantial agreement with colleagues without recourse to Star Chamber and I shall report the outcome of my bilateral discussions to the group tomorrow. A summary of the outcome for each of the main programmes which I ... shall hand out at the meeting, is attached.

3 The detailed implications of this outcome for the planning total, General Government Expenditure (GGE) and the GGE/GDP are still being worked out. As expected, the prospect is that we will publish large cash additions to GGE, even larger than in 1986. I believe that we should be able to hold the GGE ratio in 1990-91 to no more than 39 per cent. This was the figure in last year's Autumn Statement, but it will imply a small rise on this year's outturn. (This is now expected to be 38½-38¾ per cent, significantly below the figure of 39¾ per cent previously published.) Accordingly I attach great importance to achieving some decline in the ratio over the Survey period, to a level in 1992-93 no higher than that expected for this year. As things stand at present, this should just be possible.

4 The presentation of this outcome will need great care, but we can point to the continuing downward trend in the ratio, albeit at a much more modest rate, even though we cannot show a reduction in every year as we have done after other recent Surveys. Instead, the trend will be interrupted by the unexpectedly low level this year, leading to some increase in the ratio next year. Coming

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after the sharp fall in the ratio in the past few years, I believe that this outcome should enable us to demonstrate our continued determination to keep a firm grip on public spending in difficult economic circumstances.

5 You expressed a preference for making the Oral Statement on 9 November, following a discussion at Cabinet the same morning. We hope to be able to meet this timetable.



NORMAN LAMONT

S E C R E T

PUBLIC EXPENDITURE SURVEY : POSITION REACHED AFTER THE BILATERALS

Memorandum by the Chief Secretary to the Treasury

This paper reports the outcome of my bilateral discussions with colleagues, which have been conducted within the remit agreed by Cabinet in July.

The Cabinet Remit

2. Cabinet agreed that the top priority was to defeat inflation, and that the objectives for the Survey should be:

- to maintain the downward trend in general government expenditure (excluding privatisation proceeds) as a proportion of GDP;
- to stick as close as possible to existing plans.

3. These objectives are very demanding. The GGE/GDP ratio has fallen by over 7 percentage points since its recent peak in 1982-83. A combination of low spending and higher money GDP led to an unexpectedly sharp fall to 39½ per cent in 1988-89 and a further fall in the ratio is expected this year. Existing plans imply only a modest decline from now on. As John Major told Cabinet in July, the effects of lower unemployment are built into the baseline and we will not repeat last year's savings from extra receipts.

Progress in Bilaterals

4. The table at Annex A records the settlements I have been able to reach bilaterally. Annex B provides a brief description of each settlement. I am still discussing MAFP, OAL, Scotland and Wales but I expect to be able to settle them bilaterally.

5. In summary, discussions so far imply the following additions to baseline:

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| | | £ billion | |
|--|---------|-----------|---------|
| | 1990-91 | 1991-92 | 1992-93 |
| Additions agreed in Bilaterals | 5.8 | 6.7 | 10.3 |
| Aggregate External finance for local authorities (GB) | 1.3 | 1.5 | 1.7 |
| Community Charge transitional relief/safety net | 0.3 | 0.6 | 0.3 |
| Programmes still in bilateral discussion (expected outcome) | 0.5 | 1.0 | 1.2 |
| <hr/> | | | |
| Total additions to programmes | 7.9 | 9.8 | 13.4 |

Substantial as these increases are, they reflect difficult decisions by a number of colleagues on their own programmes, for which I am grateful. The original bids for programme expenditure at the beginning of September were £13/17/23½ billion, for the three years of the Survey.

SECRET

ANNEX A

AGREED PROGRAMMES

| | 1990-91 | 1990-91 | 1991-92 | 1991-92 | 1992-93 | 1992-93 |
|---|-----------|---------|-----------|---------|-----------|----------|
| | BASELINE | CHANGE | BASELINE | CHANGE | BASELINE | CHANGE |
| Ministry of Defence | 21,187.0 | 0.0 | 22,101.0 | 215.0 | 22,653.0 | 750.0 |
| FCO - Diplomatic, Information, Culture | 841.0 | 52.7 | 884.0 | 61.5 | 906.0 | 58.6 |
| FCO - ODA | 1,627.0 | 76.5 | 1,692.0 | 107.7 | 1,734.0 | 137.0 |
| Intervention Board for Agricultural Produce | 1,342.0 | -152.2 | 1,518.0 | -157.4 | 1,556.0 | -120.8 |
| Forestry Commission | 77.0 | 1.1 | 80.0 | 3.2 | 82.0 | 5.6 |
| Trade and Industry | 1,300.0 | -54.3 | 1,155.0 | -36.5 | 1,185.0 | -148.8 |
| Export Credits Guarantee Department | 122.0 | 89.5 | 61.0 | -1.1 | 63.0 | -92.2 |
| Energy | 421.0 | 24.9 | 353.0 | 41.6 | 362.0 | 30.4 |
| Department of Employment | 3,887.0 | -96.5 | 3,894.0 | -215.0 | 3,991.0 | -273.5 |
| Department of Transport | 2,645.0 | 425.0 | 2,724.0 | 525.0 | 2,792.0 | 550.0 |
| DOE - Housing | 5,737.0 | 605.7 | 6,157.0 | 569.3 | 6,311.0 | 533.6 |
| DOE - Other Environmental Services | 1,194.0 | 234.5 | 1,226.0 | 159.3 | 1,256.0 | 160.3 |
| DOE - Property Services Agency | -138.0 | 82.1 | -186.0 | 19.7 | -191.0 | -49.5 |
| Aggregate external finance for LAs* | 19,365.0 | 1,275.0 | 19,849.0 | 1,640.0 | 20,345.0 | 1,479.0 |
| Home Office (inc. Charity Commission) | 4,504.0 | 310.6 | 4,581.0 | 417.3 | 4,695.0 | 446.3 |
| Legal departments | 1,188.0 | 77.2 | 1,261.0 | 119.6 | 1,292.0 | 179.7 |
| Department of Education and Science | 5,824.0 | 781.0 | 5,932.0 | 868.0 | 6,080.0 | 861.0 |
| Department of Health and OPCS | 20,987.0 | 1,198.4 | 21,941.0 | 1,554.7 | 22,489.0 | 2,126.5 |
| Department of Social Security | 55,126.0 | 634.2 | 58,300.0 | 1,301.5 | 59,757.0 | 3,474.7 |
| Northern Ireland: negotiable | 5,855.0 | 109.8 | 5,866.0 | 146.5 | 6,013.0 | 173.5 |
| Cabinet Office, Privy Council Office, etc | 337.0 | 13.3 | 352.0 | 12.4 | 361.0 | 9.6 |
| European Communities | 1,950.0 | -85.0 | 1,580.0 | 50.0 | 1,620.0 | 450.0 |
| Nationalised Industries | -396.0 | 1,117.2 | 979.0 | 521.8 | 1,002.0 | 512.0 |
| Territorial consequences | | 662.9 | | 775.7 | | 914.0 |
| TOTAL ALREADY AGREED | 154,782.0 | 7,423.8 | 162,300.0 | 8,773.8 | 166,354.0 | 11,243.0 |

*Includes equivalent figures for Scotland and Wales. Excludes grants within AEF which are counted in other departmental programmes.

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SUMMARY OF AGREED PROGRAMMES

| | £ million | | |
|----------------|-----------|---------|---------|
| | 1990-91 | 1991-92 | 1992-93 |
| <u>Defence</u> | 0 | +215 | +750 |

The addition for 1991-92 is not new money but represents Treasury contributions towards the cost of disposal by BNFL of pre-1971 wastes agreed in last year's Survey. The addition for 1992-93 represents a 3% increase in real terms in defence expenditure over 1989-90.

FCO - Diplomatic Wing

| | | |
|-----|-----|-----|
| +53 | +62 | +59 |
|-----|-----|-----|

Increases provide for additional visa work, economic assistance for Poland, continuing UK contributions to peacekeeping forces in Iran/Iraq and Angola, scholarships and exchanges; security, relocation and overseas price movements.

FCO - ODA

| | | |
|-----|------|------|
| +77 | +108 | +137 |
|-----|------|------|

Increases provide for continued support for economic reform in Nigeria, soft loans under new arrangements for Aid and Trade Provision, and increases to bilateral aid, including forestry initiatives.

IBAP

-152 -157 -121

Reductions reflect IBAP's latest forecast of expenditure, taking account of UK and EC harvest information.

Forestry Commission

+1 +3 +6

Additions are for superannuation, forest recreational facilities, and land purchases, offset by savings on planting grants.

Trade and Industry

-54 -37 -149

The main reductions are on science and technology spending, the business development initiative, regional enterprise grants and English Estates.

ECGD

+90 -1 -92

Changes result from changed assumptions about interest rates in the UK and abroad.

Energy

+25 +42 +30

The additions provide for increased expenditure on nuclear decommissioning and radioactive waste operations; extra R&D on renewable energy sources; and the setting up of the office for regulating the electricity industry following privatisation.

Employment

-97 -215 -274

Reductions in ET and YTS reflect a tighter labour market and increased contributions from employers towards the cost of training young people. There is additional provision for the employment of disabled people, rationalisation of the Employment Service's office network, and for the new Training and Enterprise Councils.

Department of Transport

(New figures exclude BR and LHR)

+425 +525 +550

The settlement of £1.5 billion over the three years is half the level of the original bids. It is consistent with the E(A) commitment to a substantial increase in the roads programme: roads expenditure in 1990-91 will be 30% above the 1989-90 level. It will also enable DTP to fulfil its commitment to eliminate road maintenance backlogs by 1992-93. Local authority bids were cut by two-thirds. In addition, the nationalised industry figures below include an extra £1.4 billion over the 3 years for transport.

DOE - Housing

+606 +569 +534

Additions provide for substantial real increases in the Housing Corporation grant to support subsidised rented housing by housing associations, and a $\text{f}\frac{1}{2}$ billion package of measures to ease homelessness. There are technical additions of nearly $\text{f}\frac{1}{2}$ billion a year (which do not affect GGE) resulting from the reform of the Housing Revenue Account Subsidy. Offsetting savings reflect higher New Towns housing receipts and the effects of proposed real-terms increases in council rents.

DOE - Other Environmental Services

+235 +159 +160

Additions provide more support for Urban Development Corporations (particularly for transport projects in London Docklands); increased local authority credit approvals for waste disposal and methane in landfill sites; the establishment of a Climate Change Centre; increased environmental research; and more resources for the HM Pollution and Planning Inspectorates.

DOE - PSA

+82 +20 -50

For Property Holdings, additions provide for higher rents, major new works, some estate rationalisation, a further reduction in the maintenance backlog and major Parliamentary works projects; year 3 reductions reflect higher receipts. For Services, additions include IT capital expenditure, set-up costs of new design offices, and redundancy costs.

Home Office

+311 +417 +446

Settlement provides for a 10 per cent real increase in expenditure on prisons in 1990-91 (with reductions below baseline in later years to reflect lower prison population projections); additional staff for the passport department, more measures to divert offenders from custody and new anti-drugs initiatives; and a 7 per cent real growth in police grant in 1990-91 including an additional 1,100 police officers.

Lord Chancellor's and Law Officers' Departments

+77 +120 +180

For LCD, additions allow for the resource implications of the Civil and Competition Policy Initiatives, rising workloads in the county courts, and consequential for legal aid; higher accommodation charges (notably for the Crown court) and the rising cost of the court building programme, partly offset by a slow-down in new construction. For other legal departments, additions largely reflect the rising costs of major building projects.

Department of Education and Science

+781 +868 +861

Programmes agreed allow for increases between 1989-90 and 1990-91 of: 8 per cent for the Science budget on top of the large increase announced last year; 24 per cent for maintained sector capital provision - largely for schools; and 9 per cent for higher education, to finance 27,000 more student awards than previously allowed for, allow an 8 per cent increase in academic pay, and help deal with deferred maintenance. They also allow for the cost of introducing top-up student loans in September 1990.

Department of Health and OPCS

+1198 +1555 +2127

Main additions provide for the knock-on effects of the 1989 pay awards to doctors and nurses; revised forecasts of demand-led expenditure on the Family Practitioner Services; continued growth in hospital activity in response to demographic and other pressures; the costs associated with implementation of the NHS Review; increases for hospital capital expenditure; and the likely cost of pay awards in 1990-91 to non-clinical staff.

Department of Social Security

+634 +1302 +3475

Large estimating increases result in higher expenditure in 1992-93, particularly on pensioners and the disabled. Provision is also made for the impact of higher uprating assumptions. Higher benefits for poorer families and poorer pensioners, and abolition of the pensioners' earnings rule require extra provision. Expenditure on community charge benefit will be higher than on rate rebates. The net effect of changes in disability benefits will add to expenditure, particularly in later years. These increases are offset in part by the effects of lower unemployment. The Secretary of State has also decided to find savings through not uprating Child Benefit, and by tightening up the rules for recovery of maintenance from liable relatives.

Northern Ireland

+110 +147 +174

Additions include the cost of Shorts privatisation.

Nationalised Industries

+1117

+532

+512

Increased provision for British Railways and London Regional Transport will allow substantial new investment, including safety improvements. Real fares assumed to rise in 1990 by up to 3 per cent in real terms. No provision has been made for new railway lines in London. Increased provision for Post Office because of expected level of tariff increases on letters business and additional capital requirements; reductions in year 3 from British Shipbuilders from disposal of remaining yards and assets; electricity prices will rise by 6½ per cent in 1990-91.



COMPTON

12