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SUBJECT COMASTER.

10 DOWNING STREET

LONDON SW1A 2AA

From the Private Secretary

3 October 1990

Dear John,

PUBLIC EXPENDITURE

The Prime Minister held a meeting this morning to discuss the position reached in the Public Expenditure discussions. Those present were the Lord President, the Chancellor of the Exchequer, the Chief Secretary, Professor Brian Griffiths (Policy Unit), and Sir Robin Butler and Mr Peter Owen (Cabinet Office).

I should be grateful if you and copy recipients would ensure that this letter is seen only by a strictly limited number of named individuals.

Overall progress

The Chancellor said that the negotiations in the current Public Expenditure round had had to be exceptionally tough. Even if the outcome was as good as could be achieved, there would be a very large increase in the planning total.

The Chief Secretary said that bids had been even higher than in the previous year: a total of £17½ billion. This included an unavoidable element of £8½ billion for social security uprating, agricultural support, housing subsidy, local authority finance, some review body awards and other already agreed or technical items. After drawing down the reserve, it seemed likely that the addition to the planning total would be about £10 billion; to achieve even that it would be necessary to reduce discretionary bids by 60-80 per cent.

Individual programmes

Good progress had been made with the Department of Trade and Industry (which had settled slightly below baseline), the Department of Transport and the Northern Ireland Office, which were both expected to settle shortly. Reasonable progress had also been made with the Scottish Office, the Welsh Office, the Department of the Environment, the Department of Social Security and the Department of Health.

Difficult but slow progress was being achieved with the Department of Employment. He was looking for cuts in this programme, in particular to accommodate increased emphasis on TECs. The Prime Minister said that reductions in this programme should be achievable.

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The Chief Secretary said that the Foreign and Commonwealth Office had submitted a very large bid for manpower - an increase of over 16 per cent next year, rising to 32 per cent by 1993/94 - which seemed unjustifiable. The Prime Minister said that an increase on this scale would not be acceptable.

The Chief Secretary said that Education and Science had submitted the largest percentage bids of all, comprising a bid of £1 billion for polytechnics and universities, which was inappropriately based on the average rather than the marginal cost of additions to student numbers, and an increase in credit approvals for local authorities, notwithstanding the large increase in local authority spending on capital in recent years. The Prime Minister commented that the fall in construction industry prices should lead to a bigger volume of output from existing allocations.

The Chief Secretary said that the Home Office was seeking increases in respect of pay and equipment for the police. The bid for equipment represented an increase of 50-60 per cent; that was unaffordable. He was also unpersuaded by the Home Secretary's argument that it was necessary to announce a further annual increase of 1,000 in police numbers at the Party Conference.

The Prime Minister said that she had been extremely disappointed by the management and leadership of the police. It was clear that increases in resources were not an effective way of improving their performance.

The Chief Secretary said that he was looking to the Ministry of Defence for savings of £1.2 billion in year two and £2 billion in year three of the survey period to reflect the implementation of the announced Options exercise. The Secretary of State had argued that the scope for savings was offset by increased inflation and problems in aligning plans with cash provision. However the bids assumed an increase in non-pay costs 1 per cent above the GDP deflator, which was inappropriate at a time when defence manufacturers were desperate for orders. And the Ministry of Defence had consistently failed to meet the normal year-on-year efficiency targets which were routinely achieved by other departments.

The Prime Minister said that she agreed that the Chief Secretary should continue to press for savings in this programme, but that resources for the Gulf forces should be protected.

Child Benefit

The Chief Secretary said that there was a particular difficulty in the case of child benefit. A full uprating would not be affordable. On public expenditure grounds it would be preferable to have no uprating at all, but this was not politically realistic. The Secretary of State for Social Security had helpfully proposed an uprating for the first child only. This would reduce the cost, though it would be contentious with groups such as the Roman Catholic Church, who would argue

that it discriminated against larger families. No legislation would be needed.

The Prime Minister said that this was a sensitive area since families with young children had done less well than other groups in recent years. One way of tackling that problem might be by improving their tax position. A limited uprating of child benefit would have to be very carefully prepared and presented. Consideration might be given to smaller upratings for the first two children rather than an uprating for the first child only.

Presentation

The Chancellor of the Exchequer said that the presentation of an increase in the planning total of some £10 billion in mid-November would be difficult in market terms. It would be expected that it would lead either to tax increases or to a return to a borrowing requirement, and indeed current projections suggested that it was likely that there would be a return to a public sector borrowing requirement in 1991/92. It would be essential to argue that it was necessary to hold firm, and not to make panic reductions.

The Chief Secretary said that, although £10 billion was a very large sum, it represented only some 5 per cent of total public expenditure of £190 billion; this was roughly in line with the GDP deflator. It would also be possible to point out how high a proportion of the bids which had been conceded was unavoidable.

The Prime Minister thought that it should be possible to be more upbeat in presenting the increase. It was only about half the increase in the RPI and showed that the Government was not prepared to accommodate inflation.

Star Chamber

The Chief Secretary said that it was not yet certain that it would be necessary to set up a Star Chamber. Likely candidates to appear before the committee if it was set up were the Department of Education and Science, the Home Office and the Department of Employment. It would be essential, if the Star Chamber were set up, to ensure that a tougher settlement was achieved than would otherwise have been possible. Even if the resultant savings were small in macro-economic terms they would be important to maintain the credibility of the system.

The Prime Minister said that it should be a matter of principle that those who went to the Star Chamber should not do better than if they had settled in bilaterals: that would be unfair to colleagues who had already settled. The members of the committee would need to be senior Ministers who had settled. At the moment the most likely candidates appeared to be Mr Parkinson, Mr Clarke and Mr Wakeham, together with perhaps Mr Brooke or Mr Lilley. She saw advantages in having a territorial Minister as a member of the Committee.

Autumn Statement

The Chancellor of the Exchequer said that the Autumn Statement would need to be in the week of 12 November, after Parliament had reassembled but before electricity privatisation. It would be desirable to avoid a delay between the Cabinet discussion and the announcement. The precise details of timing could be settled later.

I am copying this to the private secretaries of the Ministers attending and to the others present.

Yours ever,
Barry

(BARRY H. POTTER)

John Gieve, Esq.,
H.M. Treasury.