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CABINET  
MINISTERIAL COMMITTEE ON ECONOMIC STRATEGY

NATIONALISED INDUSTRIES'  
INVESTMENT AND FINANCING REVIEW.  
STEPS TOWARDS SETTING 1982-83 EFLs  
AND LATER YEAR DECISIONS

Memorandum by the Chief Secretary, Treasury

At E Committee on 31 July we agreed that the industries as a whole should be allowed £750 million from the Contingency Reserve in each of the three years of the Review, in addition to the amounts provided in Cmnd 8751 and that sponsor Ministers should agree with the industries how the reductions in their bid, indicated in annex III of my paper E(81)79 should be brought about. These reductions amounted to £1750 million in 1982-83, £2500 million in 1983-84 and £2250 million in 1984-85. The Committee also agreed that in looking for reductions, the priority should be working capital, current costs and fixed investment in that order; and that in the context of current costs attention should be paid to the scope for savings through more realistic assumptions for increases in the pay bill. We also agreed that the industries should be told that the Government would hold investment approvals for 1982-83 to the 85% figure agreed last year until detailed plans for delivering the required savings had been produced.

2. This paper reports the industries' initial reaction to the request for reductions. It has been carried out at the same time as their normal updating of the forecasts made for IFR purposes. The position is set out in the table below:-

1.

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	£m cash		
	82-83	83-84	84-85
Baseline (Cmnd 8175 revalued)*	1040	59	63
plus Contingency Reserve allocation	+750	+750	+750
Required reductions (E(81) 26th meeting)	1750	2500	2250
Agreed reductions to date	-441	-646	-279
<hr/> Remaining excess	1309	1854	1971

The position for individual industries is set out in Annex A.

3. As I warned in my earlier paper, the updated forecasts point to some deterioration in the underlying position of individual industries which has added to the problem. The industries particularly affected are the British Gas Corporation, the British National Oil Corporation and the British Railways Board. BGC's cash flow forecasts, in the absence of remedial action, would have deteriorated by £200m in 1982-83, £350m in 1983-84 and £550m in 1984-85. As a result of a fall in projected industrial sales: these falls have been offset by remedial measures totalling about £170m, £270m and £400m in 1982-83, 1983-84 and 1984-85 respectively. In addition the £100m allowance in 1982-83 for expenditure on the gas gathering pipeline has been omitted, following the decision not to proceed with the project. These cuts still leave the industry well short of the targets agreed by E Committee on 31 July (the external financing figure for the two later years has in fact increased since the Investment and Financing Review). As a result of reduced oil production forecasts for certain fields, BNOc is faced with a

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\*The White Paper baseline has now been revalued on a revised assumption of a 9 per cent price increase between 1981-82 and 1982-83, as against the 7 per cent assumed in the Investment and Financing Review. Because of the small net external financing figures assumed in the White Paper, this change in the assumptions makes little difference to the overall arithmetic (it raises the baseline by £20m, £1m and £1m in the three years respectively).

deterioration in cash flow equivalent to £4m, £77m and £80m in each of the three years. BNOc has been able to find cuts which no more than offset this, the latest forecasts thus remaining the same as those included in the Investment and Financing Review. British Rail have identified savings of £95m in 1982-83, but a further deterioration in trading prospects has offset all but £26m of this. (Estimates for the later years take no account of the follow-through effects of the measures identified for 1982-83, or of any further measures.) The other surface transport industries have been in a broadly similar position, but have for the most part been able to deliver reductions which more than offset the deterioration in prospects, at least in 1982-83.

4. This underlying deterioration in the position of several industries means that the figures in the table above for reductions so far agreed understate the extent of the action which the industries have agreed to make by approximately £300m, £500m and £700m in the years 1982-83, 1983-84 and 1984-85 respectively. But equally it in no way diminishes the need for further savings to enable the external financing figures agreed by E Committee to be achieved.

5. The willingness of industries to deliver reductions clearly varies markedly. The major contributors to the net total so far achieved have been the National Coal Board, the National Bus Company and British Shipbuilders and (in 1982-83 only) the South of Scotland Electricity Board, the British Gas Corporation, British Airways, British Rail and the National Freight Company. On the other hand the large "savings" scored for the National Coal Board in the later years derive simply from substituting the Cmnd 8175 figures for the industry's bid and in no way represents detailed plans.

6. It is also disappointing that so little progress has been made in securing savings from reductions in working capital or cuts in current costs. Of the £440m saving agreed in 1982-83, over half (about £260m) represents a cut in fixed assets, £120m in reductions in working capital and other capital requirements and only £60m in

improvements in internal resources, including cuts in current costs. The position is broadly similar in the later years, although masked in the aggregate figures by the unspecified NCB savings. This is the reverse of what we want to see.

7. For individual industries, the process of adjustment to make the savings we require will be painful. But some industries have already made that effort. I cannot accept that others should not be required to do so. The Electricity Supply Industry in England and Wales and the Post Office have made no contribution at all and the bid from British Telecom has actually increased, as the industry has withdrawn some of the savings agreed in the IFR. Further savings are essential, especially on current costs, including pay. If the industries cannot find them, we would be unable to avoid damaging cuts in other expenditure programmes.

8. On pay, sponsor Ministers were asked to look particularly at the scope for more realistic assumptions for increases in the pay bill. The settlement levels now being assumed by the industries are set out in Annex B together with the implied percentage increases in the pay bill. Although some reductions have been made since July, the figures show a general level of settlements greatly in excess of the 4% figure and in some cases above the 4-8% which the CBI are expecting in the private sector. If industries all achieved pay increases at, or around, 4% in 1982-83, an additional £600m would be saved compared with their current bids. It would be unhelpful and unrealistic to seek to achieve this by imposing a uniform figure on the nationalised industries without regard for individual negotiating circumstances. On the other hand we should expect a lower general level of settlement in view of the present pay climate. Following the Prime Minister's meeting on 7 September sponsor Ministers have already been asked to approach Chairmen on pay. The excessive financing bids set out in this paper make it important that they should do so without delay.

### Next steps

9. We must make further progress in securing the necessary reductions before we come to take our public expenditure decisions at the end of October. I propose therefore that sponsor Ministers should have further discussions with their industries on the basis agreed in July and report the outcome to me by 2 October. They should remind the industries that without detailed plans for reducing their bids as indicated the Government will, as we decided, hold back investment approvals beyond levels approved last year. Depending on the results of these further exchanges, I may need to have further discussions with individual sponsor Ministers before reporting to colleagues collectively.

### Conclusion

10. I invite the Committee:

- (i) to note that the reductions proposed by the industries so far fall far short of what is necessary in the light of the decisions taken at E Committee in July;
- (ii) to ask sponsor Ministers to hold urgent discussions with their industries with a view to securing the additional savings necessary, in particular a reduction in the current assumptions adopted on pay, and to report the outcome to me by 2 October.

L.B.

HM TREASURY  
21 September 1981

## NATIONALISED INDUSTRIES : TOTAL EXTERNAL FINANCE

ANNEX A

Preliminary Assessment

£million outturn prices

Industry	1982-83				1983-84				1984-85			
	Figure in Investment and Financing Review	Latest forecast	Figure implied by E Committee decision, 31 July	Remaining Gap	Figure in Investment and Financing Review	Latest forecast	Figure implied by E Committee decision, 31 July	Remaining Gap	Figure in Investment and Financing Review	Latest forecast	Figure implied by E Committee decision, 31 July	Remaining Gap
NCB	1320	1100	1026	74	1404	620	973	-353	1318	672	962	-290
BC & B's	-219	-219	-653	434	-339	-339	-975	636	-335	-335	-860	525
BGC	192	99	-2	101	-60	48	-341	389	-252	-90	-482	392
BNOC	-60	-60	-120	60	-62	-62	-132	70	57	57	-13	70
BSC*	350	350	269	81	350	350	217	133	350	350	203	147
BT	516	545	297	248	543	585	222	363	509	638	244	394
FO	27	27	-133	160	-8	-8	-242	234	-13	-13	-206	193
Girobank	4	-	-8	8	-	-4	-18	14	-1	-4	-16	12
BS	147	130	121	9	136	110	95	15	88	71	44	27
BAB	86	44	43	1	124	114	51	63	99	94	18	76
BAA	61	72	48	24	55	71	37	34	35	107	20	87
BBB	1044	1018	909	109	1097	1158	992	166	1168	1229	971	258
BTTB	-5	-7	-8	1	-5	-10	-10	-	-6	-11	-11	-
KFC	-	-10	-10	1	-	-10	-16	17	3	3	-16	19
KBC	82	71	70	1	89	74	69	5	87	86	65	21
FMB	41	36	38	-2	44	39	40	-1	46	41	43	-2
NSH-EB	51	49	38	11	44	43	26	17	48	34	33	1
SSEB	265	216	230	-14	280	274	228	46	242	256	200	56
STC	26	26	23	3	29	30	24	6	30	32	25	7
TOTAL (including gas levy)	3928	3487	2178	1309	3721	3094	1240	1854	3473	3217	1224	1993
less effect of gas levy	455	430	455	-25	454	460	454	6	447	469	447	22
TOTAL (excluding gas levy)	3473	3057	1723	1334	3267	2634	786	1848	3026	2748	777	1971

\* In the absence of returns for the British Steel Corporation, the same figures have been assumed as in the Investment and Financing Review.

NATIONALISED INDUSTRY PAY 1982-83

	IFR Sett- lement Assumption	Revised settlement Assumption	Forecast increase in 1982-83 pay bill
National Coal Board	-	10.0	4.5
Electricity Boards	10.0	10.0	8.9
NS Hydroelectric Board	13.0	13.0	N/A
SS Electricity Board	10.0	10.0	N/A
British Gas Corporation	10.3	8.0	8.9
British National Oil Corporation	11.0	12.7	
British Steel Corporation	N/A	N/A	N/A
British Telecoms	14.0	11.0	12.5
Post Office	14.0	8.0	6.0
British Airways Board	10.8	8.6	0.8
British Airports Authority	9.5	10.0	5.9
British Railways Board	8.3	8.3	6.7
British Transport Docks Board	9.6	7.0	6.5
British Waterways Board	9.5	7.5	7.5
National Freight Co Ltd	7.0	7.0	14.5
National Bus Company	7.0	7.0	1.0
Scottish Transport Group	7.5	7.5	1.5
British Shipbuilders	7.0	7.0	7.7