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E(82) 8th Meeting

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CABINET

MINISTERIAL COMMITTEE ON ECONOMIC STRATEGY

MINUTES of a Meeting held at
10 Downing Street on
THURSDAY 11 MARCH 1982 at 5.00 pm

PRESENT

The Rt Hon Margaret Thatcher MP
Prime Minister

The Rt Hon William Whitelaw MP
Secretary of State for the
Home Department

The Rt Hon Sir Keith Joseph MP
Secretary of State for
Education and Science

The Rt Hon Michael Heseltine MP
Secretary of State for the
Environment

The Rt Hon David Howell MP
Secretary of State for Transport

The Rt Hon Baroness Young
Chancellor of the Duchy of Lancaster

The Rt Hon Sir Geoffrey Howe QC MP
Chancellor of the Exchequer
(Item 1 only)

The Rt Hon Peter Walker MP
Minister of Agriculture, Fisheries
and Food

The Rt Hon Patrick Jenkin MP
Secretary of State for Industry

The Rt Hon Leon Brittan QC MP
Chief Secretary, Treasury

The Rt Hon Norman Tebbit MP
Secretary of State for Employment

The Rt Hon Cecil Parkinson MP
Paymaster General

ALSO PRESENT

The Rt Hon Nicholas Edwards MP
Secretary of State for Wales

SECRETARIAT

Mr P L Gregson
Mr D J L Moore

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1. PRIVATE INVESTMENT IN CONSTRUCTION

The Committee considered a Memorandum by the Secretary of State for the Environment (E(82) 22) on private sector investment in construction projects in the public sector.

THE SECRETARY OF STATE FOR THE ENVIRONMENT said that, in conjunction with the Chief Secretary, Treasury, he had reviewed the direct involvement of market finance in construction projects in the public sector. There was a powerful case for action by the Government to stimulate activity in the construction industry, which represented about 20 per cent of total industrial production. Real output in the industry had fallen by 20 per cent from 1979 to 1981; unemployment had risen above 400,000, 25 per cent of the industry's workforce; the loss of skills and of capacity could have seriously damaging effects in all sectors when order books picked up. New investment in construction would bring much needed improvements to the country's housing stock, infrastructure, industrial buildings and inner cities. As described in his memorandum, there were already a wide range of schemes in operation, or under consideration, for encouraging more private financing, in conjunction with public sector finance, of construction. The measures, relating to the construction industry, announced by the Chancellor of the Exchequer in his Budget statement on 9 March would be helpful, but the Government still needed to do much more to ensure that existing schemes were operated effectively and that further schemes were urgently developed. He invited the Committee to endorse the principles for involving the private sector further in construction projects, as discussed in E(82) 22 and subject to the criteria set out in Annex B. He recommended that all Ministers responsible for construction programmes should review urgently the opportunities for associating private finance with their programmes on the lines he had illustrated, subject to consulting the Chief Secretary about the terms of specific proposals. He proposed that the Chief Secretary should, in association with himself and the other Ministers concerned, exercise a general oversight of these initiatives. If the policy were to be developed effectively it would be necessary to change present attitudes and to persuade the private sector of the Government's willingness to encourage private sector financing of construction projects. He recommended,

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therefore, that there should be a public statement which would make clear that the Government was ready to direct its construction policies towards securing the maximum involvement of the private sector and to consider sympathetically any proposals to this end on the understanding that the objective was to seek genuine partnerships, involving a due element of risk borne on properly competitive terms.

THE CHIEF SECRETARY, TREASURY, said that he agreed with the recommendations of the Secretary of State for the Environment, as summarised in paragraph 13 of E(82) 22, on the understanding that he would be consulted on the terms of any statement which might be made. While he was ready to examine proposals constructively and quickly, it was important to take account of the effects on the money supply and on interest rates of stimulating additional private sector financing as proposed. He attached particular importance to examining proposals for guarantees, for the introduction of private finance into public sector projects, and for the use of public expenditure to generate additional private expenditure, against the criteria set out in Annex B of E(82) 22.

THE PRIME MINISTER, summing up the discussion, said that the Committee agreed that the Secretary of State for the Environment should seek to develop the approach set out in E(82) 22 on the understanding that particular measures and projects were each examined, in consultation with the Chief Secretary, Treasury, against the criteria in Annex B of his memorandum. While the Committee wished the possibilities for further stimulation of private sector financing of construction projects to be pursued vigorously and constructively, they were not yet convinced that a significant number of projects would meet the criteria in Annex B; experience had shown that it was difficult to construct such schemes so that the private sector participants carried sufficient of the risks. They agreed, therefore, that rather than make a public statement as he had proposed, which might arouse expectations unduly, the Secretary of State for the Environment should take opportunities as they arose to draw attention to schemes already operating successfully and to the possibilities for further developments. He should agree with the Chief Secretary, Treasury on the terms of any such references to the development of the present policy. It was primarily for

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the Secretary of State for the Environment to develop such proposals but it was open to other Ministers responsible for construction programmes to put proposals on these lines to the Chief Secretary, Treasury and to consult the Secretary of State for the Environment.

The Committee -

1. Endorsed the principles for involving the private sector further in construction projects as discussed in E(82) 22 and subject to the examination of particular measures and projects against the criteria in Annex B of E(82) 22.

2. Invited the Secretary of State for the Environment -

- i. to be guided by the Prime Minister's summing up of their discussion in any public references to the development of the policy;
- ii. to continue to consult the Chief Secretary, Treasury on the development of the policy and on specific proposals.

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2. PRIVATE FINANCE FOR ROAD CONSTRUCTION

The Committee considered memoranda by the Secretary of State for Transport (E(82) 24) and by the Chief Secretary, Treasury (E(82) 25) on private finance for road construction.

THE SECRETARY OF STATE FOR TRANSPORT said that he wished to develop proposals for private financing of some trunk road schemes. It had been suggested that his Department should take a road scheme to the point where it was ready to go out to tender and then invite contractors to bid competitively on the basis that they would receive a royalty per vehicle using the road over a defined period rather than a capital sum. The contractor would make his own arrangements to finance construction, and possibly maintenance, and major firms had already expressed publicly their interest in such a scheme. If it proved practicable it would have the advantage of enabling a number of worthwhile road schemes to be brought forward and this would take up some of the very substantial spare capacity currently in the road construction industry. He recognised that if road traffic grew as expected the financing costs of his proposal would be higher in the longer term than conventional public finance; private sector finance was dearer and the contractor would need to take account of the risks which he was accepting. In order to put the prospective costs and benefits to a practical test, he invited the Committee to agree that he should develop his proposed scheme, in consultation with the Treasury, and with the road construction industry, and should then invite competitive tenders for one or two schemes on both the conventional and proposed 'royalty' bases of road financing. If his proposed scheme were to go ahead it would have to be on the understanding that the capital expenditure incurred by the private sector did not count as part of the trunk road programme for public expenditure purposes; the royalty payments would be public expenditure but would not be significant within the present Public Expenditure Survey period. He was willing to look further at private financing based on toll schemes but this would be possible only in a few instances and would require complex legislation before it could go ahead.

THE CHIEF SECRETARY, TREASURY, said that he had considerable doubts over the scheme proposed by the Secretary of State for Transport. As the Secretary of State acknowledged, it would be more expensive in the longer term and there was no virtue in holding down public expenditure in the

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short term while building up potentially greater commitments for the future. It was not clear that the scheme would bring any offsetting benefits by way of gains in efficiency. While he would be willing for officials to consider the proposal further, he would also like them to consider alternatives including those suggested in paragraphs 6-9 of E(82) 25, for letting the private sector recoup construction costs not from royalty payments from the Government but from tolls, and for devising a new tendering system for all schemes which was more closely geared to the market's demand for roads.

THE PRIME MINISTER, summing up the discussion, said that the Committee doubted whether the private sector would be willing to participate in a scheme on the lines proposed by the Secretary of State for Transport without guarantees or unacceptable limitations on the risks to them. It had been suggested, however, that there might be some gain in efficiency if account was taken of experience in the United States of America and the scheme was such as to ensure that private sector participants had an incentive to carry out maintenance at times which kept the road fully open as much as possible. The Committee agreed that the Secretary of State for Transport and the Chief Secretary, Treasury should consider the proposals set out in their memoranda and any other alternatives against the criteria in Annex B of the Secretary of State for the Environment's memorandum on private investment in construction, E(82) 22, and with a view to reaching agreement by early in the week beginning 22 March on the next steps. If they were to agree to consultations on possible schemes with the private sector, the outcome of those consultations should be further reported to the Committee who would then decide whether the proposed schemes could go ahead.

The Committee -

Invited the Secretary of State for Transport and the Chief Secretary, Treasury, consulting the Secretary of State for Industry as necessary, to discuss further the alternatives, including those set out in their memoranda E(82) 24 and 25, for private sector financing of road schemes, with the aim of reaching agreement by early in the week beginning 22 March on the next steps, and to be guided by the Prime Minister's summing up of their discussion.

Cabinet Office

12 March 1982