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THE PRIME MINISTER

13 November 1980

Dear Sir Monty,

You wrote to me on 16 October at the request of your affiliated Chambers of Commerce and Industry expressing concern at what is happening to British manufacturing industry.

I recognise that many parts of British industry are facing a difficult transitional period at the present time. However, we are convinced that the long-term interests of British industry are best served if Government economic policy continues to give priority to the control of inflation and the creation of a climate favourable to enterprise. No other policies can create the conditions necessary to achieve a sustained recovery in output and employment.

You suggest four ways in which the Government might help to reduce the pressure on industry. First, you called for lower interest rates. I am all too conscious that the current level of interest rates is placing a heavy burden on industry, and the Government would like to see an early reduction just as much as your members would. But our first priority must be to secure a further reduction in the rate of inflation. To cut interest rates while the money supply is still growing too fast would risk a resurgence in inflation and would mean throwing away the success we have already achieved on that front. We will not hesitate to cut MLR just as soon as monetary conditions permit; and to help make it possible, we are determined to contain the level of government borrowing.

/ Secondly, you

Secondly, you suggest the Government should reduce taxes on employment. The Chancellor will of course consider this suggestion very carefully in preparing for his next Budget. But I am sure you are aware that any such reduction would have to be financed by an unwelcome increase in personal taxation; or else it would mean still higher government borrowing. I would also point out that the relative tax and contribution burdens on employment of labour are lower in the United Kingdom than in our major partners in the European Community.

Thirdly, you suggest rates on industrial and commercial property should be reduced. I recognise that the recent large increases in industrial and commercial rates have been very unwelcome to industry. The new block grant system for which provision is made in the Local Government, Planning and Land Bill, will enable us to exercise much greater control over the totality of local government spending than in the past. It will also, unlike the present Rate Support Grant system which favours big spenders, provide a very strong disincentive against overspending. This should help to moderate significantly increases in industrial and commercial rates in future years. We shall also keep the interests of industrial rate payers fully in mind during the present review of the future of the rating system. Furthermore, we are doing all we can to bring home to local authorities that if they push up industrial rates, this can only put at risk jobs and new investment.

Fourthly, you say we should reduce energy costs. An important component in the increase in cost of materials and fuels has of course been the near doubling of world oil prices over the past eighteen months. Adjusting to this is a painful process for all the industrialised countries. The EEC countries are all committed to the principle of economic pricing of energy and we have been keeping close watch on price relativities between countries during the period of adjustment and in particular the difficulties - which go much wider than comparative industrial costs - resulting from continued oil and gas price controls by the United States. We are determined to achieve the maximum efficiency in the nationalised energy industries so as to keep down costs. We shall also take action where our industries are being harmed by subsidised energy prices abroad - the case of the Dutch glasshouse industry is already being referred to the European Court. The CBI and others have been preparing their own fuel price comparisons and I look forward to seeing the results of these shortly.

I know that companies in the private sector are facing a very difficult period, but I hope your members and affiliated Chambers will accept that we are doing all we can to ensure that our policies towards the public sector help in the battle to get inflation down. The measures announced at the time of the Budget mean reductions in public expenditure of £5 billion in the current year, £8 billion next year and £11 billion in the year after that. As a result we are planning for a progresive reduction in the volume of public expenditure over the next four years. I have also made it clear that we intend to reduce the size of the Civil Service, which was about 732,000 when we came to Office, to about 630,000 over the next four years.

Like you, I have been very glad to see some signs of moderation in pay settlements in parts of the private sector. For our part, we are determined to achieve lower settlements in the public sector. This is why we have made it clear that the provision for pay increases in the RSG cash limit in 1981-82 will be 6 per cent, and that the provisions in other cash limits will be dealt with broadly within the same financial disciplines. The recent announcement of the suspension of the Civil Service Pay Agreement provides clear evidence of our determination to ensure that pay is determined by decisions on cash limits.

I welcome your Association's support for our efforts to lower the rate of inflation and hope you and your members will understand from what I have said in this letter why we are determined to stick to our present policies.

Yours sincerely

Margaret Thatcher

Sir Monty Finniston, F.R.S.