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PUBLIC EXPENDITURE, 1981-82 to 1983-84

Memorandum by the Chief Secretary, Treasury

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1. In this paper I set out proposals designed to maintain the net expenditure totals for 1981-82 to 1983-84 published in Cmnd 7841, but to allow some reordering to deal with the industrial and social problems created by the recession. This is in line with our discussion on 3 July (CC(80) 27th Conclusions, Minute 5).
2. The particularly difficult year is 1981-82, with the prospect of a high public sector borrowing requirement (PSBR) and severe financial difficulties for industry. We must therefore look especially critically at our expenditure plans for that year.

TIMETABLE

3. We should settle in July our policy on local authorities' current expenditure in 1981-82, with a view to a statement before the Recess. This is the last opportunity to exercise an effective influence, and totals for individual services in 1981-82 need to be settled before mid-September so that the implications for block grant distribution can be worked out in time for the November Rate Support Grant settlement. We also need early decisions on the nationalised industries' figures for 1981-82 as a basis for setting their external financing limits, and decisions by end-September on local authority capital for 1981-82.
4. Final decisions on the other programmes do not have to be reached until October. If the outlook then shows serious financial problems we may have to look again at the expenditure totals, which for the time being we aim to maintain. By then the decisions on local authorities and nationalised industries will have foreclosed major areas; if further adjustment is needed the burden will fall on the other, mainly central Government, programmes. We should keep this in mind in considering the decisions on local authorities and nationalised industries.

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5. Decisions on the years after 1981-82 are not so urgent, but it will be convenient to take them also in the autumn.

THE PUBLIC EXPENDITURE TOTAL

6. As the Prime Minister said in the House, it is vital that the reductions in our contribution to the European Community (EC) should be used to reduce public expenditure, the PSBR and interest rates. Therefore we must plan now on keeping within the totals already agreed and published in March, as reduced by the EC savings.

7. The expenditure figures we are now considering in "1980 Survey prices" will be substantially increased by the time we get to 1981-82 by pay and price movements which have already taken place, and others yet to come. Pay and price increases generally are important to the PSBR because of their impact on the economy at large, but we must be particularly concerned with the relative development, above all of pay, between the public and private sectors. My proposals assume that the relative increase in public sector pay due to the catching-up awards of the past year will be halted. On this basis we can for the present talk sensibly around the figures in 1980 Survey prices used in this paper, and leave discussion of pay and cash limits until later, perhaps until November. But each percentage point by which the movement of public service pay in the next pay round is higher or lower than I have assumed will affect expenditure in 1981-82 by £275-300 million - equivalent to about £200 million in 1980 Survey prices.

8. The effect of the recession on the nationalised industries is at the centre of our problems in this Survey. The four major loss-makers (coal, rail, steel and shipbuilding) are in difficulties in keeping on the course embodied in Cmnd 7841, but also because of substantial additional bids for telecommunications investment and financing. The industries' Investment and Financing Review, which we shall discuss in the Ministerial Committee on Economic Strategy on 9 July, will give an opportunity to discuss measures to keep down their financing needs. Until we have considered policy papers on the loss-makers, I have assumed provisionally that the shortfall previously allowed for will not occur. That adds nearly  $\frac{1}{2}$  billion to the public expenditure totals, within which to accommodate increases on some industries and reductions on others.

9. On top of this, in a few mainly demand-led programmes some increases in expenditure will have to be accepted without full offset. So, while my general approach is to ask colleagues to absorb pressures for extra expenditure within the totals already agreed, some net reductions must be made.

10. The further cuts we have agreed in Civil Service numbers should provide additional savings, provided they are not offset by contracting services out to the private sector. But the net savings will not be available in full until

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the end of the period and in some programmes will offset increases in other expenditure. With the important exception of defence, I have carried forward the 2½ per cent cut being made this year (this amounts, over all programmes excluding defence, to some £55 million a year), but I have taken no account of the further savings in my proposals at Annex A. I shall want to look at this again in the light of the Lord President of the Council's report (which we are to discuss before the end of the month) on where the savings are to be made.

11. We shall need to consider the size of the contingency reserve later. Without prejudice to whatever decisions we eventually take on the upratings of child benefit, we should now make provision in the social security programme for those upratings, and in the employment programme for the special employment measures. The money thus freed in the contingency reserve is likely to be needed to cope with pressures arising from the recession and to provide for some flexibility in end-year expenditure.

### IMPLICATIONS FOR PROGRAMMES

12. Accordingly I propose that we plan for the time being on the basis of the net changes from the plans in Cmnd 7841 listed in Annex A. References to specific measures are elaborated in the Survey report (C(80) 38).

### LOCAL AUTHORITIES

13. It is crucial for our policy that local authorities reduce their expenditure as planned. We are taking steps to bring them into line in 1980-81. The further reductions planned for 1981-82 onwards must also be obtained. If a Minister feels it unavoidable to increase the provision for local authority spending on the services for which he is responsible I propose that he should find offsetting savings on his other programmes.

### DEFENCE

14. The growth of the defence programme cannot be unrelated to prospects for the economy as a whole, or to what we can manage in other fields. The proposal in Annex A is to base the 3 per cent growth on the likely outturn in 1979-80. This permits a saving of about £140 million a year in the plans published in March. This would offset the increase in the relative cost of this programme since those plans were determined. When we look at the plans again for final decision in the autumn, we may have to consider further whether we can afford to maintain this rate of growth for defence, which is matched by few of our allies.

### INDUSTRY

15. Substantial estimating increases on demand-led programmes have arisen here. It may not be possible to offset them all by reductions within the programme. A net increase of some £40 million in 1981-82 is probably

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inevitable, apart from any bids on the contingency reserve we may need to consider as a result of industrial problems, for example on Rolls-Royce or British Leyland.

### TRADE

16. The foreign borrowing which the Civil Aviation Authority need to finance their air traffic control investment, and which would previously not have scored against the public expenditure planning totals, should now be accepted as an addition.

### EMPLOYMENT

17. It would be right in present circumstances, and in line with our discussion last week, to provide for some net increase in the employment programme. I have therefore provided for the continuation of the special employment measures beyond next April, and for further expenditure on the youth unemployment programme. I hope the Secretary of State for Employment will be able to help by making some offsetting savings but we cannot expect, with rising unemployment, to offset the whole amount within his programme. A net increase of some £30 million in 1981-82, rising to £70 million in 1983-84, probably needs to be accepted.

### EDUCATION

18. We need to look to this programme to contribute some net savings, in addition to those required to offset the loss of the school transport measure. It should be possible to make savings of £50 million in 1981-82 and £75 million in later years, mainly on capital expenditure, higher education and a small adjustment in the school-leaving age (allowing pupils nearing their 16th birthday the option of leaving in the summer). This would partially offset the increase in the relative cost of this programme (reflecting the teachers' pay increase) since we last determined our plans.

### HOUSING

19. We also need further savings from this programme, even though our plans already envisage a substantial reduction from recent levels. I propose reductions of some £65-80 million a year (2-3 per cent) by seeking larger rent increases and cutting the provision for housebuilding and improvement.

### HEALTH SERVICE

20. Some income on which we had counted to reduce the net health programme has been lost or is in danger. We must ask the Secretary of State for Social Services to take such steps as are necessary to make alternative savings, even if, regrettably, this means some temporary reduction in standards until expansion can be resumed.

SOCIAL SECURITY

21. We should now make explicit provision in this programme for uprating child benefit annually from November 1981 in line with prices, without prejudice to our eventual decisions. The cost is some £75 million in 1981-82 rising to £360 million in 1983-84. We cannot afford to go further than that, and we should resist pressures to do so.

22. But we must seek some contribution to our problems from this very large programme, despite the considerable political difficulties. The savings proposed for this programme in Annex A could be achieved in part by once again holding back the next (November 1981) uprating on benefits covered by the Social Security (No 2) Bill by another 5 per cent, and holding back all other benefits except retirement pensions and child benefit by  $2\frac{1}{2}$  per cent. These would, inevitably, be controversial. Nevertheless justification for holding back the uprating will be reinforced if, as we expect, earnings in the next year or so rise more slowly than prices in this country, as already has been happening elsewhere.

SCOTLAND, WALES AND NORTHERN IRELAND

23. The usual formula would indicate proportional changes for Scotland, Wales and Northern Ireland. But there is evidence that the share of expenditure per head of population, taking into account assessed need, has been higher in Scotland and Northern Ireland than in Wales and England. I have agreed with the Ministers concerned that we should take account of this when deciding the allocation of additions or reductions. I do not propose an extra reduction in the programme for Northern Ireland this year, but I suggest an extra reduction of £150 million a year in planned Scottish programmes. Applying the results of the Needs Assessment Study to 1980-81 indicates that a readjustment of planned expenditure to enable each country to provide the same level of services would entail a reduction in Scotland of some £300 million. The limitations of the Study make it unwise to treat the conclusions as precise, but a reduction of half the amount indicated seems justifiable. This would also largely offset the increase in the relative cost of the Scottish programmes since we last determined our plans.

CONCLUSION

24. The result of these proposals would be that we would just about maintain the totals we published in Cmnd 7841, as reduced by the EC savings.

25. Accordingly I propose that we:

- i. Confirm that we now plan on keeping to the net totals for 1981-82 to 1983-84 published in Cmnd 7841, as reduced by the EC settlement.

ii. Agree that, subject to i. , I should discuss with any Minister who so wishes the net reductions and additions shown in Annex A.

iii. Decide before the Summer Recess the totals for current local authority services in 1981-82 so that a statement can be made to the local authorities.

iv. Agree that I should come back to Cabinet in the autumn with final proposals on the remaining programmes.

W J B

Treasury Chambers

4 July 1980

## CHIEF SECRETARY'S PROPOSALS

Net changes compared with survey baseline  
(last White Paper revalued and  
adjusted for subsequent decisions)

	£m 1980 survey prices		
	<u>81-82</u>	<u>82-83</u>	<u>83-84</u>
Price: continued 3% growth, ie increases of 6%, and 12½% on 1979-80 outturn	-135.0	-139.0	-143.0
(Total): carry forward of 2½% manpower squeeze from 1980-81	-2.0	-2.0	-2.0
British Council addition agreed by Ministers on June	+1.1	+2.2	+2.8
	-0.9	+0.2	+0.8
DAFS/WOAD: effect of revised economic assumptions, carry forward of 2½% manpower squeeze from 1980-81, and other estimating changes	-26.0	-22.6	-27.6
EC price fixing, EC fishing aid, fisheries protection and Thames barrier, largely offset by reductions suggested in PESC report	+1.5	+4.3	-7.1
	-24.5	-18.3	-34.7
Industry Commission: carry forward of 2½% manpower squeeze from 1980-81 and probable sales resulting from review	-9.0	-14.0	-12.0
Industry:			
Effect of revised economic assumptions, carry forward of 2½% manpower squeeze from 1980-81, and other reduced requirements	-44.9	-20.5	-1.9
Estimating increases in shipbuilding and steel redundancies and in regional selective assistance, and ad hoc contribution to the ECSC	+87.8	+37.3	+6.4
Steel rundown upgradings agreed by E(EA)	+16.0	+16.0	+16.0
Partially offset by reductions suggested in PESC report	-18.0	-20.0	-18.0
	+40.9	+12.8	+2.5
Industry: carry forward of 2½% manpower squeeze from 1980-81	-0.2	-0.2	-0.2
Industry: carry forward of 2½% manpower squeeze from 1980-81 and other reduced requirements	-1.4	-1.6	-2.1
Foreign borrowing	+13.0	+13.0	+13.0
	+11.6	+11.4	+10.9
Industry: net estimating changes	+25.0	+5.0	-36.0

	<u>81-82</u>	<u>82-83</u>	<u>83-84</u>	
<u>Employment:</u>				
carry forward of 2½% manpower squeeze from 1980-81 and estimating changes on demand-led services	+11.0	+5.7	-4.8	eff
special employment measures	+45.0	+85.0	+105.0	ass
youth unemployment	+18.4	+21.1	+21.1	reg
reductions in MSC g-in-a, other special measures, staff reductions	-45.0	-55.0	-55.0	chi
	+29.4	+56.8	+66.3	hold
<u>Transport: carry forward of 2½% manpower squeeze from 1980-81</u>				
	-2.0	-2.0	-2.0	cov
<u>DOE (housing):</u>				
effect of revised economic assumptions and other reduced requirements*	-90.0	-92.0	-103.0	hold
reductions in subsidies, new building and improvements	-65.0	-81.0	-71.0	ret
	-155.0	-173.0	-174.0	add
<u>DOE (PSA): carry forward of 2½% manpower squeeze from 1980-81</u>				
	-1.9	-1.9	-1.9	Civil
<u>DOE (other): carry forward of 2½% manpower squeeze from 1980-81</u>				
	-1.3	-1.3	-1.3	Scott
<u>Home Office: carry forward of 2½% manpower squeeze from 1980-81 (excluding prisons)</u>				
	-2.0	-2.0	-2.0	eff
<u>Lord Chancellor's Dept: carry forward of 2½% manpower squeeze from 1980-81, plus bids less offsetting savings proposed</u>				
	-1.0	-0.5	-0.8	car
<u>DES:</u>				
carry forward of 2½% manpower squeeze from 1980-81	-2.0	-2.0	-2.0	198
school transport loss	+37.0	+47.0	+52.0	est
reductions in higher education and student awards, school leaving age, capital expenditure, etc	-85.0	-120.0	-125.0	ass
	-50.0	-75.0	-75.0	red
<u>OAL: carry forward of 2½% manpower squeeze from 1980-81</u>				
	-1.0	-1.0	-1.0	Dep
<u>DHSS (HPSS): effect of revised economic assumptions</u>				
	+3.1	+3.1	+3.2	North

\* On Treasury assumptions about breakdown of single housing line.

<u>83-84</u>		<u>81-82</u>	<u>82-83</u>	<u>83-84</u>
	<u>WSS (social security):</u>			
-4.8	effect of revised economic and demographic assumptions, carry forward of 2½% manpower squeeze from 1980-81, and other reduced requirements	-38.0	+87.0	-16.0
+105.0	child benefit - uprating by prices	+75.0	+250.0	+360.0
+21.1	hold back 1981 uprating by 5% for benefits covered by Social Security No. 2 Bill	-35.0	-100.0	-100.0
-55.0	hold back other benefits (apart from retirement pensions and child benefit) by 2½%	-25.0	-60.0	-60.0
+66.3	additional savings - various possibilities	-50.0	-90.0	-120.0
-2.0		-73.0	+87.0	+64.0
	<u>Civil superannuation: estimating changes</u>	+3.8	+4.8	-0.3
-103.0	<u>Scottish Office (excl DAFS):</u>			
-71.0	effect of revised economic assumptions, carry forward of 2½% manpower squeeze from 1980-81, other reduced requirements and estimating changes in regional selective assistance	+4.1	+4.0	-7.2
-174.0	reductions derived by formula from other Departments' figures	-11.4	-16.1	-14.8
-1.9	reductions on account of assessed need	-150.0	-150.0	-150.0
-1.3		-157.3	-162.1	-172.0
-2.0	<u>Welsh Office (excl WOAD):</u>			
-0.8	effect of revised economic assumptions, carry forward of 2½% manpower squeeze from 1980-81, other reduced requirements and estimating changes in regional selective assistance	+0.5	-0.5	-3.3
-2.0	reductions derived by formula from other Departments' figures	-3.4	-4.4	-3.9
+52.0		-2.9	-4.9	-7.2
-125.0	<u>Northern Ireland:</u>			
-75.0	effect of revised economic assumptions, carry forward of 2½% manpower squeeze from 1980-81, other reduced requirements and estimating changes in industrial development assistance	+5.1	+10.1	+10.8
-1.0	reductions derived by formula from other Departments' figures	-3.6	-3.1	-0.6
+3.2		+1.5	+7.0	+10.2

	<u>81-82</u>	<u>82-83</u>	<u>83-84</u>
<u>Smaller Departments:</u>			
carry forward of 2½% manpower squeeze from 1980-81	-17.7	-17.6	-17.6
other reduced requirements	-5.6	-4.7	-6.1
additions (largely for computers)	+4.3	+6.1	+6.8
	-19.0	-16.2	-16.9
<u>Nationalised industries' finance</u>	+470.0	+470.0	+470.0
<u>Changes already agreed since White Paper and included in survey baseline</u>	-63.8	-32.3	-78.0
<u>TOTAL of changes proposed above to plans in White Paper</u>	-114.5	+12.3	-131.1

	79-80	80-81	81-82	82-83	83-84
<u>Planning total after shortfall</u>					
White Paper revalued, as reduced by EEC savings	77830	77350	76485	74830	74375
Total of changes proposed above -	-	-	-115	+12	-131
Resulting total	77830	77350	76370	74845	74245
(Percentage annual change)	(-0.1)	(-0.6)	(-1.3)	(-2.0)	(-0.8)