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NOTE OF A MEETING BETWEEN THE PRIME MINISTER AND SIR RAY PENNOCK AT 1600 HOURS ON FRIDAY 12 SEPTEMBER 1980 AT 10 DOWNING STREET

Present: Prime Minister — Sir Ray Pennock
Mr. David Wolfson
Mr. Clive Whitmore
Mr. Tim Lankester

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Sir Ray Pennock first described the pay situation as he saw it. He had met the Chairmen of a number of major companies in early August, and had urged them to hold out for moderate settlements. The general message seemed to be getting over that no more than single figure settlements could be afforded in the coming round, and the negotiating prospects from management's stand point appeared to be better than for several years. There was a much greater realism in industry that excessive pay settlements would cost jobs. For example, two vehicle companies had made sensible offers, and BP had made an offer of 10% - though this was subject to possible review next March. But industry remained very concerned about pay in the public sector. He cited as the latest example the rejection by the local authority white collar workers of a 13% offer, and the decision by the employers to accept arbitration. There was always a tendency for arbitrators to ignore what could be afforded, and he found it difficult to understand why the employers had agreed to this course. Although the Clegg Commission was being disbanded, industry was worried that the comparability arrangements implicit in the Pay Research Unit agreement were being continued; they were also concerned about index-linked pensions, though they noted that these were being reviewed by the Committee chaired by Sir Bernard Scott. In addition they were concerned - as always - about the prospects for the miners settlement. If the NCB had to borrow from the banks, rather than from the Government, the situation might be very different.

Sir Ray went on to say that the general position of industry was not as bad as appeared from the press. Nonetheless, it was very patchy. On the one hand there were companies such as his own (i.e. BICC), and companies in the electronics and oil sectors, which were doing very well. On the other hand, many companies were

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in real difficulty. Many companies were citing the exchange rate as the main cause of their difficulties: for example, ICI had told him that even if their wages were zero, they could no longer compete in several of their product areas. There was a strong feeling in industry that if interest rates came down, the exchange rate would fall - though there was disagreement amongst bankers as to whether this would happen. As to the effect of a fall in interest rates on borrowing, many industrialists - for example, he had recently heard this in Scotland - felt that borrowing would not increase. Although the effect of high interest rates and the high exchange rate palled into insignificance compared with the effect of moderate or excessive pay settlements, interest rates - and the exchange rate - were a major concern. He wondered whether public expenditure was still too high, and whether this was the cause of the continued high interest rates.

The Prime Minister said that the Government were deeply concerned about public sector pay, and also about the high interest rate/high exchange rate problem. As to the former, pay settlements in the public sector had been more or less level pegging with those in the private sector, and both must come down. It was crucial in the coming round that public sector pay settlements did not undermine the new-found realism of the private sector. She agreed that the reported decision to take the local authority white collar claim to arbitration was worrying. As regards the miners, people would not be too concerned if a high settlement for the face workers did not go through to the surface workers; but this always seemed to happen. Much would depend upon the negotiating tactics of the NCB Chairman. The general financial position of the nationalised industries, of which pay was a part, was one of the biggest problems that the Government had to face: it was essential to the success of the Government's strategy that the resources pre-empted by the nationalised industries should be reduced. As regards PRU, she hoped that CBI members would give evidence to the Scott Committee.

Turning to the problem of high interest rates, the Prime Minister said that the main difficulty was that the banks had continued to lend to the private sector at a high level. If MLR were reduced in advance of market rates, there would almost certainly be "round-

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tripping", and this would inflate the money supply still more. It was not clear whether a small fall in interest rates would reduce the exchange rate. Nonetheless, it was essential to get interest rates down as soon as possible, and the CBI could be assured that Ministers were giving this high priority. The announcement of the new "Granny Bond" should help. Public expenditure was being kept under a tight rein, despite the huge demands of the nationalised industries. For example, the Government had set tough cash limits; a prospective overspend of £650 million on the defence programme had been cut back to £200 million; and the Civil Service was being cut.

In further discussion the following points were made:

(i) The Prime Minister said that Ministers would have to make more of the nationalised industries' problems in speeches - and of the fact that they were, by their appalling performance, doing so much damage to the economy. Public pressure had to be brought to bear upon nationalised industry managements to improve efficiency and cut costs. Sir Ray said that, while the general economic message seemed to be getting over, it would be worth emphasising the extent to which exports were now at risk if pay went up too fast in the coming round.

(ii) The Prime Minister said that she was concerned about the effectiveness of the Training and Youth Opportunities Programmes. Given the large amount being spent, it was essential that we produced the skills that were needed. Sir Ray said that many large companies had not done enough to help with the Youth Opportunities Programme, and he intended to take this up with them. He had also written to every CBI member to persuade them to absorb as many school leavers as possible.

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(iii) Sir Ray said that, largely because of trade union restrictions on apprenticeships, there continued to be a shortage of craftsmen - even at a time of deep recession. The unions controlled the whole system of apprenticeship - for example, no-one over 21 could become an apprentice - and without having completed an apprenticeship, it was impossible to obtain a union card. At the same time, we did not make full use of those who were trained because of over-manning and demarcation. There were many examples - for example in the chemical and motor industries - where British industry was obliged because of union restrictions to use far more employees than were strictly needed; and this showed up in comparative productivity figures as between the UK and other countries. Whenever he visited a plant, he always asked the manager how many men could run it if there were no union restrictions, and how many hours per day did the fitters work. The Prime Minister said that it was time the Government exposed the trade unions on both the apprenticeship and the demarcation issues. She wondered whether, on the demarcation issue, it would be worth the CBI promoting a campaign under the head of productivity or efficiency through the NEDC.

(iv) Sir Ray said that the Government ought to do more to publicise our industrial successes. There were many fine examples of British inventiveness and efficiency. The Prime Minister said she would give some examples of "success" in her Bordeaux speech.

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(v) Sir Ray said that the level of employee involvement in British industry remained abysmal. Two surveys had been carried out, one at the time of the Bullock Report, and the other last year, and the latter showed that - if anything - the situation had got worse. There was no way in which industry could be successfully managed unless problems and prospects were properly discussed with employees. Employee participation arrangements in most companies compared very badly with the arrangements for political participation available under our democratic system. He intended to bring this issue to the fore. The Prime Minister said that she might be able to help by, say, attending a CBI Council meeting and raising this issue.

(vi) The Prime Minister said she was delighted with the appointment of Sir Terence Beckett as Director-General of the CBI.

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15 September 1980