

**CONFIDENTIAL**

DOCUMENT IS THE PROPERTY OF HER BRITANNIC MAJESTY'S GOVERNMENT

C(80) 14

COPY NO

83

25 February 1980

**CABINET**

**CASH LIMITS 1980-81**

**Memorandum by the Chancellor of the Exchequer**

1. In order to reach conclusions on the size and shape of my Budget, and to publish the Estimates, I need to settle the cash provision we make for all cash limited public expenditure. We have taken decisions in most areas and need now to confirm them in the light of recent developments and of the economic prospect. But we still have to take one important decision in the area of Civil Service pay.
2. Cash limited expenditure has five separate components:
  1. The Rate Support Grant (RSG) on local authorities current expenditure, in which provision for pay and price increases was set at 13 per cent.
  2. The nationalised industries' external finance limits, where the provisions for implicit pay and price increases varied between industries, but, on average, were of about 14 per cent.
  3. The current expenditure of the central Government other than pay, for which we have set provision for price increases of 14 per cent, and the capital expenditure of central Government and local authorities for which the provision is somewhat higher.
  4. The pay in central Government other than the Civil Service (principally the National Health Service), for which we have also provided for an increase of 14 per cent; and
  5. the Civil Service pay element for which we have yet to fix the provision for an increase.

It is of high importance that we should not take action which would precipitate reopening 1. and 2. Nor do I see any need for us to do so if the cash provision for local authorities and nationalised industries is marginally less than is required. They are both able to increase income at their own

**CONFIDENTIAL**

discretion: rate increases in the case of local authorities and price increases in the case of nationalised industries. Categories 3., 4. and 5. however have only one source of income. Any shortfall in cash provision here necessarily entails a volume cut.

3. I have not yet formed a final view on the forecast of inflation to be published at the time of the Budget. There is bound to be a margin of error around these forecasts and in managing the programmes it is right to take a cautious view. I suggest that we allow in our discussion for the possibility that, on average, prices may exceed the provision we agreed for the cash limits by about 3-3½ percentage points. (In suggesting these figures I have taken as a working assumption that specific indirect taxes will be increased in the Budget in line with the movement of prices over the last year. I will comment orally on this at Cabinet.)

4. On pay, leaving aside the Civil Service on which we have a separate paper, and the armed forces for which I accept that the defence cash limit should be adjusted to accommodate the costs of our commitment to maintain full comparability, the current expectation is that new public service pay settlements may on average lead to about 15 per cent increase in earnings. The squeeze exerted by cash limits as now set will depend on the outcome of each set of negotiations. Our aim must be to keep that outcome at low as possible.

5. These considerations suggest that, save to the extent that they result in improved efficiency, the cash limits set in accordance with our previous decision would reduce the volume of the central Government and local authority capital expenditure in 1980-81 which they cover by about £500 million at 1979 Survey prices, equivalent to 2 per cent of the expenditure, plus the value of whatever cut in Civil Service manpower results from our decision on Civil Service pay.

6. The question is whether we should increase the provision so far agreed for cash limits on categories 3. and 4. on this account. My advice is that we should not, for the following reasons:

First, it would require countervailing tax increases to enable me to achieve my target for the Public Sector Borrowing Requirement in 1980-81. The further specific reductions which we agreed in expenditure programmes for 1980-81 fell some way short of the target of £1000 million which we set ourselves before Christmas.

Second, a squeeze on the scale envisaged is smaller than some which have occurred in recent years, and substantially smaller than that which occurred this year, when the general price increase allowed for in the cash limits was only 8½ per cent.

Third, increases in the provision in central Government cash limits would precipitate pressure to increase the cash limits already set and published for the rate support grant and external financing limits for the nationalised industries.

Fourth, a moderate squeeze through cash limits can be accommodated by, and is a useful spur to, efficiency and the reduction of waste.

7. There is, however, an interaction between our decision on this and our decision for category 5., ie Civil Service pay. If we decided that we had to provide more than 14 per cent for Civil Service pay increases, it would become much harder to resist arguments for an increase in the provision so far agreed in cash limits generally. Taking account of the Clegg and other comparability awards and of the staging of other past awards, provision of 14 per cent now would mean that between 1979-80 and 1980-81 the total public service paybill is likely to rise by some 24 per cent. We cannot afford to add to this figure by making the provision now under discussion more than 14 per cent.

#### CONCLUSION

8. I invite Cabinet to confirm our earlier decision that the 1980-81 cash limits for central Government expenditure and for local authority capital expenditure should incorporate provision for a 14 per cent increase in current expenditure costs, and the slightly higher provision as previously agreed for capital expenditure. (This excludes Civil Service pay which is the subject of a separate paper; and the Rate Support Grant for which our previous 13 per cent decision already announced stands). Each Minister should so manage the expenditure for which he is responsible as to keep within the cash limit so set, adjusting the volume programme so far as may prove necessary.

G H

Treasury Chambers

25 February 1980