c Master set
Agriculture - Milk Prices
cc Mr Ingham.

CONFIDENTIAL

Euro Pol TN

10 DOWNING STREET

From the Private Secretary

5 December 1979

The Prime Minister held a meeting at 1450 hours today to discuss various proposals relating to agriculture. The following were present: your Minister, Chancellor of the Exchequer, Chief Secretary, Secretary of State for Trade, Sir Robert Armstrong and Sir Kennith Berrill.

The Prime Minister said that the purpose of the meeting was to reach a preliminary view in advance of Cabinet the following day on three issues: first, whether or not to undertake a devaluation of the green pound in the immediate future; second, whether, and if so by how much, to increase the maximum retail price of milk; third, what to do about farm capital grants. The paper prepared by the official group under the chairmanship of Sir Kenneth Berrill provided a very helpful background. It was necessary to devise a package which would balance the interests of the farming community against the need to restrain public expenditure and consumer prices - taking into account also our EEC interests. She herself was disposed to a five per cent green pound devaluation immediately, and some increase in the price of milk which she hoped could be kept to no more than 1p per pint. But she wanted to have other Ministers' views on these two issues, and also on the question of capital grants.

The Secretary of State for Trade said that he was in favour of a five per cent devaluation immediately, a 1p increase in the price of milk, and a reduction in the level of grants as proposed by the Treasury. He favoured an immediate devaluation on non-agricultural grounds. It was important for our negotiating stance in the EEC that we take action now rather than in the New Year when we would be pursuing a strong line with the EEC to reduce Community surpluses. It would be damaging if at that time the farming lobby were to be complaining that more needed to be done for them. As regards capital grants, he recognised that subsidies in Europe were generally greater than in the UK. But agricultural investment in the UK had been at a very high level. There was some evidence that grants had encouraged more investment than was necessarily desirable. Production of milk in particular had been over-stimulated, and so indirectly had borrowing from the banks. As for milk prices, some increase was clearly necessary, and this should take place immediately; but the increase should be no more than 1p.

/The Chief Secretary

CONFIDENTIAL

The Chief Secretary then commented on the question of grants. There were in his view four arguments in favour of the reduction which he was proposing. First, Government grants to industry were being cut back, and to be equitable, the same should happen in respect of agriculture. Second, as a matter of principle, it was inappropriate for farmers to derive their incomes from grants; it was better that they should obtain their income from adequate prices. Third, the extra capital expenditure which resulted from grants stimulated agricultural production at a time when we were intent on reducing surpluses. Fourth, there was some evidence - while our agriculture was generally efficient - that we were having to pay a high price for extra production. Marginal costs of UK agriculture were higher than in other EEC countries because our production at the margin was highly capital intensive.

Your Minister said that the need for a five per cent devaluation, a 1½p increase in the milk price, and an increase in capital grants, was borne out by the table in paragraph 61 of the official group's report. This showed that, even with the devaluation and the milk price increase, farmers' net income would be lower in 1980 than it was this year; and it had to be borne in mind that the level of incomes this year was substantially lower than it had been in 1978. The Tory Party had strongly criticised the previous Government for allowing incomes to fall as far as they had done in 1978. To do less than he was proposing would be highly damaging politically. The farming community would take particular offence at any cutting of capital grants at a time when other countries in Europe were increasing their subsidies to agriculture. The increase in grants which he was proposing was needed partly to compensate farmers for the reduction in income which they would suffer even with the five per cent devaluation and the 1½p milk price increase. There was also a strong economic argument for assisting agriculture at this time. In contrast to industry, agriculture was almost totally free from restrictive practices and could be depended upon to respond to extra incentives; this would benefit national output and the balance of payments.

As regards milk, Mr. Walker pointed out that if the price increase were held back, this would simply mean that a bigger increase would be necessary at some later date. Producers were going to be hard hit by the recent award by the Agricultural Wages Board, and the dairies' costs were likely to be rising fast too. The Prime Minister questioned whether the distribution of milk was as efficient as it might be. The official group's report suggested that the dairies' distribution costs were unnecessarily high. Moreover, there was the question of whether milk ought not to be available in the shops at a lower price than it was on the doorstep. The housewife should surely, as in other countries, be able to buy milk at a lower price in the shops than through the door-to-door delivery system. She understood that in Scotland more milk was sold in the shops and at a cheaper price than on the doorstep.

/Mr. Walker responded

Mr. Walker responded that milk buying habits in Scotland had long been different from what they were in England. There was nothing to stop the food retailers from buying milk direct from the Milk Marketing Board in England and bottling and retailing it themselves. However, it did not appear to be economic. More generally, he had to warn colleagues that if any action was taken which might put an end to the door-to-door delivery system, this would have very damaging effects on milk consumption and hence production - with important political implications. If a significant number of people switched to purchasing milk in shops, the door-to-door system would no longer be viable. The Prime Minister commented that she could not accept that the present distribution system would necessarily collapse if more milk were sold in shops; and in any case, she could not see that the Government and consumer should necessarily support production of milk at its current level. Finally, the timing of the next price increase ought, if possible, to take into account prospective month-to-month fluctuations in the RPI.

Summing-up, the Prime Minister said that it was generally agreed that there should be an immediate devaluation of the green pound, though of course this would need to be endorsed by Cabinet. No agreement had been reached on milk prices and capital grants: these questions would need to be discussed further in Cabinet.

I am sending copies of this letter to Tony Battishill (Treasury), Alistair Pirie (Chief Secretary's Office), Stuart Hampson (Department of Trade), George Walden (Foreign and Commonwealth Office) and Martin Vile (Cabinet Office).

T. P. LANKESTER

SP

G.R. Waters, Esq.,
Ministry of Agriculture, Fisheries and Food.