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*Agriculture*

Ref. A03731

PRIME MINISTER

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E: Liquid Milk Prices

BACKGROUND

✓ — In his letter to you of 27th November the Minister of Agriculture, Fisheries and Food proposes that the maximum retail price of liquid milk should be increased by  $1\frac{1}{2}$ p per pint from 21st December. Since January 1978 the Government have fixed maximum wholesale and retail prices: the difference between them being the distributive margin which is intended to cover the costs of processing and distributing liquid milk, plus a target rate of profit for the dairy trade also determined by the Government.

✓ — 2. His proposal is on the agenda for tomorrow's meeting because, on present plans, E will not meet again until Tuesday, 16th December. Depending on the line taken by the Chief Secretary, Treasury, it is probable that agreement can be reached on the proposed December increase without any lengthy discussion. The Secretaries of State for Wales (1st December), Scotland (2nd December) in minutes to you and the Secretary of State for Northern Ireland in a minute to the Minister of Agriculture (3rd December) have all said they agree. We do not know what is the Chief Secretary's line, but his officials may advise him to question whether the increase should be less, on the grounds that while the producers may need something more the distributors' case is weaker. Some Ministers may also raise longer-term issues which will be relevant to further increases in 1981; and the Secretary of State for Northern Ireland has raised the fundamental question whether there should be a phased withdrawal from Government control by ceasing to control the wholesale price.

✓ — 3. At their meeting on 6th August the Committee approved an increase of  $\frac{1}{2}$ p in August rather than the  $1\frac{1}{2}$ p then proposed by the Minister of Agriculture (E(80) 30th Meeting, Item 2). They agreed that any further increases should be considered after the Binder Hamlyn report on the liquid milk costing system had been considered and in the light of any action which the Monopolies and Mergers

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Commission (MMC) might propose if there were a referral of milk distribution. It was also agreed that the timing of the increase would have to take account of the timing of CAP price fixing negotiations and of movements in the RPI.

4. The increase now proposed is less than the industry wants but would generate additional revenue of £45 million this financial year in England and Wales. It is held that this is necessary to help both the producers (and check further falls in the size of the dairy herd) and the distributors who might otherwise have to cut services.

5. The Minister of Agriculture would argue that it is for other EC members to reduce their milk surpluses. We are not self-sufficient and all the proposed price increase will do is to check a further fall in production at a cost to the balance of payments. It would lead to an increase of 0.15 per cent on the RPI and of 0.7 per cent on the Food Price Index. 21st December is proposed, after consultation with the Department of Employment, so that the increase would be in the January RPI which should be lower than that for December.\* Some savings should emerge from the second Binder Hamlyn report which is now being received, but these will have to be negotiated and MAFF think that they will not have much impact in the present financial year. The Director General of Fair Trading is considering a reference to the MMC on milk distribution. He will not make proposals until January, and it will then be for decision whether the Secretary of State for Trade should allow such a reference to go ahead. Milk prices are usually increased twice a year and further consideration of the Binder Hamlyn report, and of any report by the MMC, together with examination of any other longer-term issues, will therefore be relevant to the proposals which will be coming forward for increases in 1981.

6. The present proposal does not appear to raise European Community issues. An increase on 21st December would be well clear of negotiations on the Commission's 1981 price proposals. Any effect of this proposal on FEOGA expenditure (see paragraph 2 of the Annex to the letter) would be trivial in relation to total FEOGA expenditure. Officials are looking separately (in EQO (legal)) at the Commission's challenge to our health restrictions - the Chief Secretary's letter of 2nd December refers.

-2-

\*The Secretary of State for Employment now proposes 3rd January (cf. his minute to you of 3rd December).

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7. As in August, the Minister of Agriculture has not consulted the other Ministers directly concerned, or authorised any general discussion at official level, before minuting you. If he had undertaken such prior consultations, he would then be in a position to advise whether his proposals commanded general support and to bring out any differences of view; and it might not have proved necessary to discuss the issue in E. You may like to say, for the record, that in future he should undertake prior consultations with the other Ministers directly concerned before coming to E (or Cabinet).

#### HANDLING

8. There will probably be little time left for discussion of this item. I suggest that you put two main questions to the Committee:

- (i) Does any member dissent from the proposal that there should be an increase of  $1\frac{1}{2}$ p on 21st December? Mr. Prior thinks that it should be on 3rd January.
- (ii) What points should be registered for the longer term and in preparation for proposals for increases in 1981?

The question of a reference to the MMC will be considered in January.

Departments may wish to discuss with the Ministry of Agriculture the implications of the Binder Hamlyn report.

These further discussions could also take account of any other proposals for changes in the arrangements, including that by the Secretary of State for Northern Ireland, for phasing out the system of price controls. Other Ministers will wish to give their reactions to the latter but it should not be necessary to go into these longer-term issues in any detail tomorrow. They could be looked at later on the basis of a full analysis.

9. The Minister of Agriculture might be invited to arrange for interdepartmental discussion of the longer-term issues before he comes forward with his next proposal for an increase.

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CONCLUSIONS

10. In the light of the discussion you will wish to record conclusions:-
- (i) Endorsing the proposed increase of  $1\frac{1}{2}$ p per pint on 21st December, or any alternative agreed.
  - (ii) Commissioning further work on any longer-term issues identified and requiring this to be completed before the next proposal for an increase.
  - (iii) Inviting the Minister of Agriculture to arrange for full interdepartmental discussion of both longer-term issues and particular price proposals prior to submission of recommendations to the Committee.

RA

ROBERT ARMSTRONG

3rd December, 1980