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38th  
Sessions

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CABINET

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CONCLUSIONS of a Meeting of the Cabinet  
held at 10 Downing Street on  
TUESDAY 4 NOVEMBER 1980  
at 10.00 am

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PRESENT

The Rt Hon Margaret Thatcher MP  
Prime Minister

The Rt Hon William Whitelaw MP  
Secretary of State for the Home Department

The Rt Hon Lord Hailsham  
Lord Chancellor

The Rt Hon Lord Carrington  
Secretary of State for Foreign and  
Commonwealth Affairs

The Rt Hon Sir Geoffrey Howe QC MP  
Chancellor of the Exchequer

The Rt Hon Sir Keith Joseph MP  
Secretary of State for Industry

The Rt Hon Francis Pym MP  
Secretary of State for Defence

The Rt Hon Lord Soames  
President of the Council

The Rt Hon James Prior MP  
Secretary of State for Employment

The Rt Hon Sir Ian Gilmour MP  
Privy Seal

The Rt Hon Peter Walker MP  
Minister of Agriculture, Fisheries and Food

The Rt Hon Michael Heseltine MP  
Secretary of State for the Environment

The Rt Hon George Younger MP  
Secretary of State for Scotland

The Rt Hon Nicholas Edwards MP  
Secretary of State for Wales

The Rt Hon Humphrey Atkins MP  
Secretary of State for Northern Ireland

The Rt Hon Patrick Jenkin MP  
Secretary of State for Social Services

The Rt Hon Norman St John-Stevas MP  
Chancellor of the Duchy of Lancaster

The Rt Hon John Nott MP  
Secretary of State for Trade

The Rt Hon David Howell MP  
Secretary of State for Energy

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The Rt Hon Mark Carlisle QC MP  
Secretary of State for Education and Science

The Rt Hon John Biffen MP  
Chief Secretary, Treasury

The Rt Hon Angus Maude MP  
Paymaster General

THE FOLLOWING WERE ALSO PRESENT

The Rt Hon Norman Fowler MP  
Secretary of Transport

The Rt Hon Michael Jopling MP  
Parliamentary Secretary, Treasury

SECRETARIAT

Sir Robert Armstrong  
Mr P Le Cheminant  
Mr D J L Moore

SUBJECT

PUBLIC EXPENDITURE 1981-82 TO 1983-84

The Cabinet considered memoranda on public expenditure by the Chief Secretary, Treasury (C(80) 58), by the Chancellor of the Exchequer and the Chief Secretary, Treasury (C(80) 64), and by the Secretary of State for Scotland (C(80) 62). They also had before them a letter on the same subject from the Minister of Transport to the Chancellor of the Exchequer dated 27 October.

The Cabinet's discussion and conclusions reached are recorded separately.

Cabinet Office

4 November 1980

CABINET

LIMITED CIRCULATION ANNEX

CC(80) 38th Conclusions

Tuesday 4 November 1980 at 10.00 am

The Cabinet considered a memorandum by the Chief Secretary, Treasury (C(80) 58) and a memorandum by the Chancellor of the Exchequer and the Chief Secretary, Treasury (C(80) 64) proposing changes in public expenditure programmes.

THE PRIME MINISTER said that, continuing the discussion begun at its previous meeting, the Cabinet now had to reach specific decisions on the cuts to be made in public expenditure. In a brief general discussion, it was suggested that the Cabinet should not necessarily accept the case for "equality of misery" in considering cuts in public expenditure on economic grounds, without having due regard also to the political and social consequences of what was proposed. The Cabinet should be in a position to weigh the economic, political and social consequences of all the various means of achieving the Government's economic strategy, including changes in taxation as well as reductions in public expenditure. It was suggested that final decisions should not be reached on any of the proposals now before the Cabinet until there had been an opportunity of considering all of them. It was also pointed out that it was a major objective of Government policy to reduce the burden of public expenditure upon the resources generated by the private sector: this was achieved by reductions in public expenditure but not by increases in taxation which transferred resources from the private to the public sector.

The Cabinet then turned to the detailed proposals set out in C(80) 64.

THE CHANCELLOR OF THE EXCHEQUER said that in further discussion with Departmental Ministers agreement had been reached on reductions in the programmes of the Department of the Environment, the Ministry of Transport, the Foreign and Commonwealth Office (including Aid), and of the Office of Arts and Libraries.

THE SECRETARY OF STATE FOR THE ENVIRONMENT said that in order to make the cuts required of him from the Housing Programme, and to avoid any further reductions in capital investment, it was likely that the rent guideline for next year would have to indicate an average rent increase of £3.25 compared with the £2.85 implied by the figures in the last Public Expenditure White Paper (Cmd 7841). This was likely to be presented as discrimination against the council house tenant as against the home owner who enjoyed tax relief on his mortgage interest, the increase would of course be mitigated for those tenants eligible for the rent rebate scheme. It would also have an inflationary effect and, taken in conjunction with other factors (such as increases in rates and in electricity and gas prices), would be used to justify higher pay claims than otherwise. So far as possible he would look for revenue rather than capital cuts on the other part of his programme.

THE PRIME MINISTER, summing up this part of the discussion, said that the Cabinet took note of the implication for council house rents of the proposed cuts in the Housing Programme. All those Ministers who had already agreed to make the full cuts demanded of them would be faced with strong public criticism. Their difficulties in rebutting this criticism would be considerably increased if similar cuts were not made on other programmes.

The Cabinet -

1. Endorsed the agreed reductions in public expenditure programmes reported in C(80) 64.

THE CHANCELLOR OF THE EXCHEQUER said that he proposed a further 1 per cent cut in local authority current expenditure in each year, to be shared out proportionately among the relevant programmes, on top of the decision announced in August of a 2 per cent reduction. Of this further 1 per cent cut, £61 million would fall on the education services. In addition he recommended that in 1981-82 the cash limited higher education programmes should be cut by 2 per cent, as was proposed for cash controlled programmes generally, at a cost of £30 million; rather than by  $\frac{1}{2}$  per cent, or £8 million, as proposed by the Secretary of State for Education and Science. The total cuts for 1981-82, including the £85 million agreed by Cabinet in July, should be carried forward by reductions of £236 million in 1982-83 and of £241 million in 1983-84.

THE SECRETARY OF STATE FOR EDUCATION AND SCIENCE said that, if the proposed cut of £61 million were implemented the total reduction in current expenditure on the education services would be about  $4\frac{1}{2}$  per cent between 1980-81 and 1981-82, compared with a fall in the number of pupils in the year of only 2 per cent. This would be contrary to the assumption, which had previously been

accepted, that the fall in expenditure could not match that in pupil numbers without reducing standards. Of the £85 million reduction agreed in July, \$ 63 million was off local authority current expenditure. Of the total cut of £124 million which was now demanded he judged that about £100 million would have to come from the schools programme. This sum was twice the total annual provision for books; and equivalent to about two-thirds of the provision for education of children under the age of 5. In practice it would have to be found by increasing the reduction in teacher numbers to 26,000 in the year compared with the 11,000 assumed at present. Redundancies would not help because of the costs involved in redundancy payments, and in practice local authorities would have to suspend the recruitment of teachers and would be unable to replace any teacher leaving in the next 12 months. This would add to the difficulties already arising from shortages of mathematics and science teachers. In his judgment such reductions in the numbers of teachers were not feasible within this timescale. Already local authorities, including Conservative controlled authorities, were complaining strongly of the cuts so far required of them. Anything more would be highly damaging to the Government, both politically and in terms of its education policy.

In discussion the following points were made:-

a. An exception for the education services would make it impossible to achieve a cut in local authority current expenditure by a further 1 per cent. It would be tantamount to saying that the Government now judged that education merited higher priority than, for example, the law and order services. In practice under the new grant arrangements it would be for the local authorities to decide for themselves how the cuts would be made and on the proportion which would fall on the education services.

b. It did not necessarily follow that the proposed reduction would affect educational standards. If the cuts were implemented, there would be a 4 per cent decline in expenditure between 1979-80 and 1981-82 compared with a 6 per cent reduction in pupils. Only about half of staff expenditure was on teachers. Some authorities had been vigorous in reducing non-teaching staff but there remained room for further savings in this area by other authorities. On the teaching side, teachers had benefited from two recent high pay awards; and the number of unemployed teachers had remained stable at a time when unemployment generally was rising, although this partly reflected the reduced intake of people into the teacher training colleges.

THE PRIME MINISTER, summing up this part of the discussion, said that the Cabinet recognised the difficulties of making further cuts in the education programme. Without them, however, it would not be possible to achieve the 1 per cent reduction in local authority current expenditure which was a major ingredient of the proposals for reducing public expenditure. The proposed £61 million cut in current expenditure on education services should therefore be accepted as part of the general 1 per cent cut on local authority current expenditure, subject to the other proposals before the Cabinet for reductions in local authority current expenditure also being agreed.

The Cabinet -

2. Agreed to a reduction of £61 million in 1981-82 in current expenditure on education services, as part of a general 1 per cent cut on local authority current expenditure, subject to agreement being reached on the other components of the 1 per cent cut.
3. Agreed to resume discussion later of the proposed 2 per cent cut in cash controlled educational spending programmes.

THE CHANCELLOR OF THE EXCHEQUER said that he accepted that it would not be possible to make good the £100 million loss of income from health charges, mainly for accidents, which could not now be implemented. He recommended that, in addition to the cut on local authority current spending on social services which had already been agreed, there should be a reduction of £126 million representing the health programme's share of the general 2 per cent reduction in cash controlled programmes. He did not agree with the alternative of raising this sum by an increase in the National Health Service (NHS) element in the National Insurance contribution. This would reduce the Public Sector Borrowing Requirement (PSBR) but not public expenditure. It was essentially a form of tax, and a regressive poll tax at that, and, if an increase were to be considered, it should be in the context of a review of all the options for changes in taxation.

THE SECRETARY OF STATE FOR SOCIAL SERVICES said that there had already been reductions in the net cost of the health programme from increased prescription charges; and reductions in expenditure from reorganisation and greater efficiency were already in train, though the full financial benefits of this would not accrue until after 1981-82. He strongly recommended that, rather than make any further expenditure cuts in spending on the NHS, the amount required should be raised by an increase in the NHS element in the National

Insurance contribution. He would be willing to consider an increase of 0.2 percentage points, which would be sufficient to cover not only the saving which the Chancellor of the Exchequer was now seeking but also the £100 million loss of income from charges. This approach would be in line with the Government's longer term objective of placing greater reliance on insurance as a means of financing the health service. It was socially sensible, in that it placed the burden on those in work rather than (as cuts in the Service would) on the sick, the old, and the unemployed. He believed that it would be perceived by the general public not as an increase in tax but as an addition to the insurance premium for NHS care. It would avoid the alternative of cuts which could well involve closing wards and reducing the numbers of doctors and of nurses. Subject to further advice, he believed that the change could be effected without the need for primary legislation in advance of the Finance Bill or of other social security legislation which might be introduced next year.

In discussion it was pointed out that there was still considerable inefficiency in the health services and that there should be some scope for finding further savings without, in effect, pre-empting tax decisions. On the other hand there would be difficulty in finding such savings quickly, and the proposed increase in the NHS charge would avoid the major social and political difficulties which would result from further cuts in the health programme.

THE PRIME MINISTER, summing up this part of the discussion, said that the Cabinet agreed on balance that the NHS element in the National Insurance contribution should be raised rather than the health programme cut. The Secretary of State for Social Services should consider further whether this decision posed any difficulties for the legislative programme, and he should consult further with the Chancellor of the Exchequer on what should be the yield sought from the increase in the contributions.

The Cabinet -

4. Agreed that there should be an increase in the National Health Service element in the National Insurance contribution rather than a cut in health expenditure.
5. Invited the Secretary of State for Social Services:
  - a. to consult further with the Chancellor of the Exchequer on the extent of the increase;
  - b. to confirm that the decision would not require early primary legislation;

and to report.



THE CHIEF SECRETARY, TREASURY, said that to provide for special employment measures he recommended net increases of £167 million in 1981-82, £203 million in 1982-83 and £189 million in 1983-84. These proposals assumed that the Secretary of State for Employment would find £42 million net savings in 1981-82, and rather more in the later years, in addition to his share of the general 2 per cent cut in cash limited programmes and the 1 per cent cut in local authority current expenditure. This additional provision would be sufficient to finance continuation, but not improvement, of existing special employment schemes and undertakings, including the Youth Opportunities Programme (YOP).

THE SECRETARY OF STATE FOR EMPLOYMENT said that the additional provision necessary to maintain existing schemes and undertakings arose in part because of rising unemployment and in part because the Job Release Scheme (JRS) and the Temporary Short-Time Working Compensation Scheme (TSTWCS) had previously been financed from the Contingency Reserve. The Chief Secretary, Treasury's, proposals, implying no improvement of existing schemes, represented not an increase in expenditure but merely a transfer from the Contingency Reserve. At a time when unemployment was rising rapidly it was not sufficient simply to maintain existing schemes. Some modest improvement was necessary to help in particular the young and the adult long-term unemployed. A further £15 million in 1981-82 would enable him to make significant improvements in the YOP particularly directed to 16 and 17 year olds. To increase the opportunities for the longer term adult unemployed he wished to replace the regionally based Special Temporary Employment Programme (STEP) by a new nationwide Community Enterprise Programme (CEP). CEP should be able to provide for 25,000 people compared with 12,000 under STEP. It would recognise the problems of the high pockets of unemployment outside the development areas. It would be developed in partnership with private sector industry and voluntary agencies. The additional costs would be £28 million in 1981-82. He proposed that the TSTWCS, which helped firms avoid redundancies, should give support in future for up to 9 months rather than 6 months at present. He was prepared to offset the costs of this extension by reducing the rate of support from 75 per cent to 65 per cent of normal pay. He was reluctantly prepared to forego any improvements in the JRS and in this way additional expenditure of £46 million in 1981-82 would be avoided.

In discussion it was suggested that further consideration should be given to the inter-relation between the measures proposed by the Secretary of State for Employment and measures for industrial assistance for which the Department of Industry and the Department of the Environment (through the Development Commission and the Council of Small Industries in Rural Areas (COSIRA)) were responsible, so as to eliminate duplication and overlap.

THE PRIME MINISTER, summing up the discussion, said that the Cabinet agreed to the improvements in special employment measures proposed by the Secretary of State for Employment and to the proposed change in the TSTWCS, and agreed to forego improvements in the JRS. The Chief Secretary, Treasury, should now discuss these changes, and the net offsetting savings which he had proposed, further with the Secretary of State for Employment and reach agreement on the total net additions to the employment programme in each year.

The Cabinet -

6. Invited the Chief Secretary, Treasury, and the Secretary of State for Employment to agree on the total net additions to the employment programme in the light of the Prime Minister's summing up of their discussion.

7. Invited the Secretary of State for Employment to discuss with the Secretaries of State for Industry and for the Environment the inter-relation between his proposals for special employment measures and measures for regional and industrial assistance in their fields of responsibility.

THE CHANCELLOR OF THE EXCHEQUER said that he recommended reductions of £500 million in each year from the Defence Budget, made up of £188 million from the general 2 per cent cut in cash limited expenditure and of £312 million specific cuts. The effect would be to break with the aim of 3 per cent growth in defence spending in real terms in 1981-82, but this was justified against the background of our acute economic difficulties and at a time when many of our allies were also failing to meet the North Atlantic Treaty Organisation (NATO) target.

THE SECRETARY OF STATE FOR DEFENCE said that the Government had already cut £1.5 billion from the programme inherited from the last Administration, which it had criticised as inadequate. Within that reduced programme it would be necessary to finance Trident and to honour the undertaking that it would enable us to reinforce our conventional defence capability. The cuts made involved delays and cancellation of projects for all three services. The Defence Budget had already been reduced as far as he and the Chiefs of Staff judged to be prudent. Any further cuts, and failure to fulfil our NATO commitment to 3 per cent growth annually, would be damaging to the Alliance, to our international standing and to the security of the West at a time of increasing tension worldwide. Admittedly some of our allies were falling short of the target growth

in expenditure this year, but most of them could point to a better growth record in defence spending than the United Kingdom in recent years. Failure to live up to our promises could lead others to relax their efforts. Moreover, if there were to be cuts of £500 million, this would have very serious effects on the defence industrial base: he estimated that it would lead to 70,000 jobs lost, to the bankruptcy of many firms and to the disappearance of some defence industries. Cuts of this scale would be contrary to the Government's pledge in the Manifesto, and would imply an actual reduction in the level of defence spending in real terms. He was prepared to recommend as a compromise, on which he did not have the support of the Chiefs of Staff, a cut of £152 million in 1981-82, subject to three conditions:

- i. While he did not at this stage seek a commitment from the Cabinet to implement whatever the Armed Forces Pay Review Body recommended in April 1981, recognising that the Cabinet should be free to take whatever decision was appropriate when the recommendations were received, the cash limit for armed forces pay in 1981-82 should be adjusted to accommodate whatever pay increases the Cabinet agreed in the light of the Review Body's report.
- ii. The cash limit factor for prices as applied to the Defence Budget should be adjusted to take account of the fact that prices for defence equipment tended to increase faster than the general level of prices.
- iii. There should be no further changes in the base-line for the Defence Budget.

On this basis he would undertake to absorb in 1981-82 any amount by which defence expenditure in 1980-81 overran the revised cash limit for that year.

THE CHANCELLOR OF THE EXCHEQUER said that the Secretary of State for Defence's proposals failed to take account of the reality of the decline in the United Kingdom's gross domestic product or of the contribution which was needed from the Defence Budget if the agreed objective for bringing down the public sector borrowing requirement was to be achieved. The conditions proposed implied a view that the Ministry of Defence and the armed forces should be outside the disciplines imposed on the Government as a whole by the realities of the economic situation.

In discussion the following points were made:

- a. Increases of 3 per cent would have been achieved in 1979-80 and in 1980-81 and, under the Chancellor of the Exchequer's proposals, would probably be made in 1982-83 and in 1983-84. In the present economic climate

a dip in 1981-1982 would not be unexpected, at home or abroad. The cut should not be to the full extent of £500 million, since this would lead to a reduction of 0.7 per cent in the level of defence spending in real terms. It would, however, be reasonable that at the very least £188 million should be found from the Defence Budget in line with the general 2 per cent cut on other cash limited programmes. Going above this, a cut of £400 million would still allow for a 0.3 per cent increase in real spending in 1981-82. In deciding on the cut to be made it would be important to have regard to the effects on industry.

b. The Government was committed by the Manifesto to pay comparability for the armed forces. It would nevertheless be a mistake to allow for the cash limit to be adjusted on account of this or of the cost of defence equipment. The defence cash limit had been seriously overrun in 1980-81 and to provide for exceptions would be to invite a repetition of this situation. As it was, the Defence Budget alone among major programmes was allowed to take credit for staff savings.

THE PRIME MINISTER, summing up this part of the discussion, said that the Cabinet accepted that the cuts on the Defence Budget would have to be less than the £500 million which the Chancellor had sought but more than the £152 million offered by the Secretary of State for Defence, which did not even meet the requirement of £188 million representing the general 2 per cent cut in cash limited expenditure. While the commitment to pay comparability for the armed forces would stand, it remained for further consideration whether exceptions should be made on this, or any other, account in determining the cash limits for the Defence Budget. The Secretary of State for Defence should now consider urgently, with the Chancellor of the Exchequer and the Chief Secretary, Treasury, what further cuts he could offer, and report the outcome to the Cabinet as soon as possible.

The Cabinet -

8. Invited the Secretary of State for Defence to consider further with the Chancellor of the Exchequer and the Chief Secretary, Treasury, the scope for further cuts in the Defence Budget and report the outcome to the Cabinet as soon as possible.

9. Agreed to resume their discussion on public expenditure and related issues at their next meeting.

Cabinet Office

5 November 1980