



FROM: CHIEF SECRETARY  
DATE: 27 September 1984

PRIME MINISTER

**PUBLIC EXPENDITURE IN 1984-85**

At the end of last week's discussion in E(A) of my proposal for a moratorium on local authority capital spending you asked that the Chancellor and I bring forward proposals to deal with the expected overshoot on public expenditure this year. The current forecast of the overshoot is £1.25 billion, or £1.5 billion if the miners' strike goes on to the end of the year.

2 I have conducted a review of the possibilities. Although it is still open to us to take decision which would bring this year's spending closer to plan, I have concluded - in the light of the decision which we have taken on local authority capital and other issues - that the action necessary to get back to the planned figure would not be acceptable to our colleagues.

3 Numerous measures could be taken to defer expenditure, or to squeeze programmes generally this year. We could impose a moratorium on central government capital and on defence procurement, together with a cut-back on training in the armed forces, savings in the employment special measures programme, and so on. These measures could cause a great deal of disruption without large savings, and the least damaging way of squeezing programmes (as last year) would be by an across-the-Board reduction in cash limits of, say, 1 per cent (equivalent to about 3 per cent on the remaining spend this year). This would be worth about £430 million gross, or £300-350 million net after taking account of the fact that some of the reduction would have shown up anyway in underspending, and that some of the cuts might not stick.

4 Many of the individual deferments, cancellations and other savings implicit in a squeeze on this scale would, clearly, be resisted strongly by our colleagues. It seems unlikely that colleagues, who have ruled out at moratorium on local authority capital, would be ready to agree to one on their own Departmental programmes. At this late stage in the year there would be maximum opprobrium in seeking reductions in areas where it would be necessary publicly to withdraw funds already promised - for example from the Regional Health Authorities and the Research Councils (as you know, some of these are already arguing that their existing funding is inadequate).

5 These are some of the objections to an across-the-board cash limits cut. But we should, in addition, recognise the damage which would be done to the discipline of the cash limits system if - for the second year in succession - we changed cash limits in mid-year. In a year in which many cash limits are already under pressure from the extra costs of public sector pay settlements above the figure allowed for in the Estimates and from Budget VAT changes cash limit reductions would compel Departments to make cuts which make little economic or any other sense - in flat contradiction to all our efforts to improve financial management in Whitehall.

6 These considerations, in my view, rule out cash limit reductions as a practical possibility. Many of the non-cashlimit reductions which it is open to us to make - on social security, NHS charges, agricultural grants, for example - are, I believe, equally ruled out by existing pledges, or the force of political circumstances.

7 But there are some possibilities. We have already agreed in principle that the relevant costs of the miners' strike should be recovered through electricity prices once the strike is over. A decision now for a 10 per cent increase from 1 November would bring in some £250 million. I am separately considering savings on NCB investment, and from the electricity supply industry in the range of £100-150 million. If special asset sales go well (no hitches with the BT flotation, the civil aviation issue resolved satisfactorily and a number of other 'ifs' too) the proceeds may exceed our current forecast.

8 We should, in my view, pursue all these possibilities, with the objective of minimising the overspend. To that end we should severely limit any further claims on the Reserve, go hard for any savings, including increased charges, which we can identify, and accelerate asset sales and disposals of surplus public sector land whenever possible.

PK

PETER REES

How can we decide now whether strike is still continuing?