PO-CH/NL/0053

PART B

SECRET

(Circulate under cover and notify REGISTRY of movement)

PO -CH /NL/0053

PART B

1986 AUTUMN STATEMENT
BUDGET DEBATE

DD's 25 years 27-01-95 NAzig.

PO -CH /NL/0053
PART B

STARTS: 5-12-86
ENDS: -12-12-86

CLOSED

CONTINUED ON:-

PART C

ps4/3H

CONFIDENTIAL

PWP

FROM: A P HUDSON
DATE: 5 December 1986

SIR T BURNS

cc PS/Chief Secretary
Sir P Middleton
Mr F E R Butler
Mr Cassell
Mr Monck
Mr Scholar
Mr Peretz
Mr H P Evans
Mr Sedgwick
Mr Turnbull
Miss O'Mara
Mr Culpin
Mr Allan
Miss Evans
Mr Cropper
Mr Tyrie
Mr Ross Goobey
PS/Inland Revenue

AUTUMN STATEMENT DEBATE

We understand that the Autumn Statement debate is very likely to take place on Wednesday, 17 December, with the alternative being Tuesday, 16 December, though nothing has been announced in the House.

2. Since we have had the Autumn Statement, the Opposition Day debate, and the Debate on the Address all within the past few weeks, it is not easy to think of anything new to say about the economy.

3. We can make use of statistics published since the Autumn Statement, which tend to confirm the forecast. But I should be very grateful if you and copy recipients could consider whether there are any other new points to make, or new figures to comment on.

APH

A P HUDSON

FROM: A P HUDSON

DATE: 5 December 1986

CHANCELLOR

AUTUMN STATEMENT DEBATE SPEECH

1. I think it would be helpful to discuss these questions about your speech for the Autumn Statement debate.

Motion

2. Should the government motion be along the same lines as in 1985 (copy attached)?

Length

3. You spoke for a total of 30 minutes last year, and 40 minutes in 1984 when there were a lot of interventions. Should we prepare about 25 minutes worth of material this year?

Content

4. You have already mentioned two things which you would like to include:

(a) a rebuttal of the TCSC report;

(b) a reinforcement of the message about tax cuts.

5. You will presumably also want to say something about the following subjects, and it would be useful to discuss the balance between them.

(a) Monetary Policy

Not an Autumn Statement matter, but was a major feature of the TCSC report.

(b) Fiscal Policy (no PSBR increase; tax cuts off).

(c) Public Expenditure

(d) The Forecast

Particularly, perhaps, the current account

(e) The Economic Record

6. Do you want to pick up any of the other issues raised during your evidence, such as the relationship with local government, or overheating?

7. Do you want to cover any other particular topics? Looking back at the main events of 1986, possibilities include wider share ownership, charities, the Big Bang and the EC Presidency.

8. Do you want to take any particular line in attacking Labour? I am not aware of any fresh ammunition since the last debate. Since you are opening, you could pose some questions to Mr Hattersley about Opposition policies.

9. Is the attached structure about right?

APH

A P HUDSON

AUTUMN STATEMENT DEBATE: STRUCTURE

1. Quotations produced to suggest lack of continuity of policy.

2. But danger of confusion between:

   - policy objectives and intermediate targets;
   - indicators and instruments.

3. Overriding objective has always been reduction of inflation. Record shows success.

4. Always had two sides to anti-inflation policy; fiscal and monetary.

5. Fiscal policy - gradual reduction of PSBR. Cover tax cuts issue.

6. Monetary policy - set out in Lombard Speech. Stress that interest rates have always been an instrument of monetary policy.

7. Success of policy is record of steady growth and low inflation.

8. Forecast for 1987, reinforced by statistics since Autumn Statement.

9. Any particular topics (wider share ownership etc.)

10. Questions to Hattersley.

Autumn Statement 1985-86

4.15 pm

The Chancellor of the Exchequer (Mr. Nigel Lawson): I beg to move,

That this House approves the Autumn Statement presented by Mr. Chancellor of the Exchequer on 12th November; welcomes the prospect of continuing low inflation and steady growth as the basis for maintaining the trend of rising employment; and congratulates Her Majesty's Government on the continuing reduction in the share of national income pre-empted by public expenditure.

Mr. Speaker: I have selected the amendment in the name of the Leader of the Opposition.

Mr. Lawson: Let me start by apologising to the right hon. Member for Birmingham, Sparkbrook (Mr. Hattersley). In our last debate I praised the right hon. Gentleman's writings for *Punch*. I had not realised that this harmless compliment would be used by the SDP to cast doubt on the right hon. Gentleman's working class credentials. Apparently, a Mrs. Shirley Williams declared on television last week:

"You aren't working class Roy — you're a very good writer."

Could I make it clear that we on this side of the House, who do not suffer from these class hang-ups, entirely accept that the right hon. Gentleman is every bit as working class as he feels it necessary to be.

Exactly a month ago today I presented my autumn statement to the House. In it I described a satisfactory outlook for growth, inflation and the current account of the balance of payments. I set out this Government's public expenditure planes for the next three years. In the intervening month inflation has fallen back further, to an annual rate of 5·5 per cent., as I predicted, and last week's figures appear to confirm that the long and seemingly inexorable rise in unemployment has at last come to an end. The whole House will, I know, welcome this.

I have read with interest the report of the Treasury and Civil Service Select Committee. Once again, I congratulate the Committee, under the skilful chairmanship of my right hon. Friend the Member for Worthing (Mr. Higgins) on the speed with which it has been produced.

It is useful to recall what the autumn statement is and what it is not. My predecessor presented the first autumn statement to the House in 1982. It contained then, as it does now, three principal elements. The first is a projection of the Government's expenditure plans. This year I have expanded the information available on public expenditure by providing plans not just for the immediate year ahead but for each of the next three years. The second is a new forecast of economic prospects, as required by the Industry Act. The third is the rates of national insurance contributions for the coming year. That is what the autumn statement is.

It comes at the end of the annual public expenditure round and gives the House an early indication, before publication of the public expenditure White Paper, of the Government's spending plans.

The autumn statement is not and has never been a sneak preview of the budget. It is essentially for this reason that I decided this year not to publish either the so-called estimated fiscal adjustment for 1986-87 or the inevitably highly uncertain revenue forecast from which the fiscal adjustment figure could be conventionally derived. I am genuinely sorry that the Committee has not felt able to endorse this common sense decision. I found its arguments on this point distinctly unpersuasive and we shall simply have to agree to disagree. There will be no fiscal adjustment or revenue forecast published this autumn or any subsequent autumn.

Indeed, there could have been no swifter vindication of the decision not to publish a revenue forecast at the time of the autumn statement than the latest developments in the oil market, following the OPEC meeting in Geneva. The dust has not settled on that yet, and it is too soon to form a view of the likely level of oil prices during the coming year, but, in so far as the prospect now is for a lower oil price than was assumed at the time of the autumn statement, it follows that, other things being equal, tax revenues in 1986-87 will be correspondingly lower and the scope for tax reductions in next year's Budget correspondingly diminished. The House and the country should be in no doubt about that.

While it is possible to conceive of a sudden fall in the oil price so great as to cause serious disruption and dislocation to the entire world economy, I find the prospect as unlikely as it is undesirable. Short of that, there is no threat to the British economy. Even now, at its peak, oil accounts for only 6 per cent. of GDP, and we are a substantial oil consumer as well as a substantial producer. What we stand to lose on the swings, we stand to gain on the roundabouts.

Mr. Dick Douglas (Dunfermline, West): Does the right hon. Gentleman agree that he has missed out the fact that we are also a substantial oil exporter thanks to the fact that we are currently producing as much as the Saudis— *[Interruption.]* I am sorry, but we are producing 2.7 million barrels a day, which is much the same as the Saudis. The Chancellor has access to much more information than I, and I am sure that he will correct me if I am wrong. What does he predict will be the oil price in February and March next year when we are likely to be in great difficulties and his fiscal and budgetary strategy is likely to be in ruins?

Mr. Lawson: I will no more make predictions about the oil price in the spring than I will give a fiscal adjustment for 1986-87.

Government policy in this area remains unchanged. I recall a rather similar state of affairs some three years ago, when I was Secretary of State for Energy. The oil price was weak, and the nervous Nellies, if I may borrow a phrase, were talking about "free fall". OPEC decided to hold its meeting, for the first time, in London — in order, so it was said, to bring pressure to bear on Britain to curb its oil production.

I had the very great pleasure of receiving visits from several eminent OPEC oil Ministers, all of whom wanted us to do just that. I explained how that was impossible and how we in the United Kingdom maintain the freest oil province in the world in which decisions on how much to produce are made not by the Government but by the oil companies. That remains so today, and there is no way round it—not even by the back door.

As it happens, United Kingdom oil production is now at its peak, and from now on is likely to be on a gradually declining path, but there is no way in which the United Kingdom will become a country member of OPEC.

CHANCELLOR OF THE EXCHEQUER

C.

1. The attached minute follows discussion with Michael, Robert, Alex, & Carys Evans.

2. It is not seeking answers to the questions now, but intended to act as an agenda for a short meeting. So the only questions for now are:

(a) Is the agenda OK?

(b) Do you want a meeting on Tuesday/Wednesday with either a small cast (Michael, Robert, ~~Carys,~~ MOM, Carys Evans, Alex & me), or a bigger cast to include Peter, Terry, Andrew Turnbull, and the Chief Secretary?

AH

FROM: A P HUDSON

DATE: 5 December 1986

CHANCELLOR

AUTUMN STATEMENT DEBATE SPEECH

1. I think it would be helpful to discuss these questions about your speech for the Autumn Statement debate.

Motion

2. Should the government motion be along the same lines as in 1985 (copy attached)?

Length

3. You spoke for a total of 30 minutes last year, and 40 minutes in 1984 when there were a lot of interventions. Should we prepare about 25 minutes worth of material this year?

Content

4. You have already mentioned two things which you would like to include:

(a) a rebuttal of the TCSC report;

(b) a reinforcement of the message about tax cuts.

5. You will presumably also want to say something about the following subjects, and it would be useful to discuss the balance between them.

CONFIDENTIAL

(a) Monetary Policy

Not an Autumn Statement matter, but was a major feature of the TCSC report. [incorporate in 4(a)]

(b) Fiscal Policy (no PSBR increase; tax cuts off). [that is 4(b)]

(c) Public Expenditure [incorporate in 4(a)]

(d) The Forecast [probably ditto]

Particularly, perhaps, the current account

(e) The Economic Record

+ Rebuttal scene (! start)

CSO / privatisation & Gas prop? PRINT shortfalls on big bangs – Storm

6. Do you want to pick up any of the other issues raised during your evidence, such as the relationship with local government, or overheating?

7. Do you want to cover any other particular topics? Looking back at the main events of 1986, possibilities include wider share ownership, charities, the Big Bang and the EC Presidency.

Training levy

8. Do you want to take any particular line in attacking Labour? I am not aware of any fresh ammunition since the last debate. Since you are opening, you could pose some questions to Mr Hattersley about Opposition policies.

9. Is the attached structure about right?

Plus PX (£728m etc)

APH

A P HUDSON

Oppn schizophrenia

5 minute launch speeches @ end?

C15/021

AUTUMN STATEMENT DEBATE: STRUCTURE

1. Quotations produced to suggest lack of continuity of policy.

2. But danger of confusion between:

   - policy objectives and intermediate targets;
   - indicators and instruments.

3. Overriding objective has always been reduction of inflation. Record shows success.

4. Always had two sides to anti-inflation policy; fiscal and monetary.

5. Fiscal policy - gradual reduction of PSBR. Cover tax cuts issue.

6. Monetary policy - set out in Lombard Speech. Stress that interest rates have always been an instrument of monetary policy.

7. Success of policy is record of steady growth and low inflation.

8. Forecast for 1987, reinforced by statistics since Autumn Statement.

9. Any particular topics (wider share ownership etc.)

10. Questions to Hattersley.

Coming down ex this process - blip caused by loss of oil revenues

Autumn Statement 1985-86

4.15 pm

The Chancellor of the Exchequer (Mr. Nigel Lawson): I beg to move,

That this House approves the Autumn Statement presented by Mr. Chancellor of the Exchequer on 12th November; welcomes the prospect of continuing low inflation and steady growth as the basis for maintaining the trend of rising employment; and congratulates Her Majesty's Government on the continuing reduction in the share of national income pre-empted by public expenditure.

Mr. Speaker: I have selected the amendment in the name of the Leader of the Opposition.

Mr. Lawson: Let me start by apologising to the right hon. Member for Birmingham, Sparkbrook (Mr. Hattersley). In our last debate I praised the right hon. Gentleman's writings for *Punch*. I had not realised that this harmless compliment would be used by the SDP to cast doubt on the right hon. Gentleman's working class credentials. Apparently, a Mrs. Shirley Williams declared on television last week:

"You aren't working class Roy — you're a very good writer."

Could I make it clear that we on this side of the House, who do not suffer from these class hang-ups, entirely accept that the right hon. Gentleman is every bit as working class as he feels it necessary to be.

Exactly a month ago today I presented my autumn statement to the House. In it I described a satisfactory outlook for growth, inflation and the current account of the balance of payments. I set out this Government's public expenditure planes for the next three years. In the intervening month inflation has fallen back further, to an annual rate of 5·5 per cent., as I predicted, and last week's figures appear to confirm that the long and seemingly inexorable rise in unemployment has at last come to an end. The whole House will, I know, welcome this.

I have read with interest the report of the Treasury and Civil Service Select Committee. Once again, I congratulate the Committee, under the skilful chairmanship of my right hon. Friend the Member for Worthing (Mr. Higgins) on the speed with which it has been produced.

It is useful to recall what the autumn statement is and what it is not. My predecessor presented the first autumn statement to the House in 1982. It contained then, as it does now, three principal elements. The first is a projection of the Government's expenditure plans. This year I have expanded the information available on public expenditure by providing plans not just for the immediate year ahead but for each of the next three years. The second is a new forecast of economic prospects, as required by the Industry Act. The third is the rates of national insurance contributions for the coming year. That is what the autumn statement is.

It comes at the end of the annual public expenditure round and gives the House an early indication, before publication of the public expenditure White Paper, of the Government's spending plans.

The autumn statement is not and has never been a sneak preview of the budget. It is essentially for this reason that I decided this year not to publish either the so-called estimated fiscal adjustment for 1986-87 or the inevitably highly uncertain revenue forecast from which the fiscal adjustment figure could be conventionally derived. I am genuinely sorry that the Committee has not felt able to endorse this common sense decision. I found its arguments on this point distinctly unpersuasive and we shall simply have to agree to disagree. There will be no fiscal adjustment or revenue forecast published this autumn or any subsequent autumn.

Indeed, there could have been no swifter vindication of the decision not to publish a revenue forecast at the time of the autumn statement than the latest developments in the oil market, following the OPEC meeting in Geneva. The dust has not settled on that yet, and it is too soon to form a view of the likely level of oil prices during the coming year, but, in so far as the prospect now is for a lower oil price than was assumed at the time of the autumn statement, it follows that, other things being equal, tax revenues in 1986-87 will be correspondingly lower and the scope for tax reductions in next year's Budget correspondingly diminished. The House and the country should be in no doubt about that.

While it is possible to conceive of a sudden fall in the oil price so great as to cause serious disruption and dislocation to the entire world economy, I find the prospect as unlikely as it is undesirable. Short of that, there is no threat to the British economy. Even now, at its peak, oil accounts for only 6 per cent. of GDP, and we are a substantial oil consumer as well as a substantial producer. What we stand to lose on the swings, we stand to gain on the roundabouts.

Mr. Dick Douglas (Dunfermline, West): Does the right hon. Gentleman agree that he has missed out the fact that we are also a substantial oil exporter thanks to the fact that we are currently producing as much as the Saudis— *[Interruption.]* I am sorry, but we are producing 2.7 million barrels a day, which is much the same as the Saudis. The Chancellor has access to much more information than I, and I am sure that he will correct me if I am wrong. What does he predict will be the oil price in February and March next year when we are likely to be in great difficulties and his fiscal and budgetary strategy is likely to be in ruins?

Mr. Lawson: I will no more make predictions about the oil price in the spring than I will give a fiscal adjustment for 1986 87.

Government policy in this area remains unchanged. I recall a rather similar state of affairs some three years ago, when I was Secretary of State for Energy. The oil price was weak, and the nervous Nellies, if I may borrow a phrase, were talking about "free fall". OPEC decided to hold its meeting, for the first time, in London — in order, so it was said, to bring pressure to bear on Britain to curb its oil production.

I had the very great pleasure of receiving visits from several eminent OPEC oil Ministers, all of whom wanted us to do just that. I explained how that was impossible and how we in the United Kingdom maintain the freest oil province in the world in which decisions on how much to produce are made not by the Government but by the oil companies. That remains so today, and there is no way round it—not even by the back door.

As it happens, United Kingdom oil production is now at its peak, and from now on is likely to be on a gradually declining path, but there is no way in which the United Kingdom will become a country member of OPEC.

CONFIDENTIAL

FROM: A P HUDSON

DATE: 9 December 1986

PS/CHIEF SECRETARY

cc Sir P Middleton
Sir T Burns
Mr Scholar
Mr Turnbull
Mr Culpin
Miss O'Mara
Mr Allan
Mr Tyrie
Mr Ross Goobey

CHANCELLOR'S AUTUMN STATEMENT DEBATE SPEECH

... I attach the list of questions to be discussed at today's meeting on the Chancellor's speech for the Autumn Statement Debate.

APH

A P HUDSON

12.100 UNCLASSIFIED

PWP

FROM: A P HUDSON
DATE: 10 December 1986

MR DOLPHIN

cc Sir T Burns
Mr Scholar
Mr H P Evans o.r.
Mr Sedgwick
Mr S Matthews o.r.
Mr Culpin
Miss O'Mara
Mr Ross Goobey

CHANCELLOR'S AUTUMN STATEMENT DEBATE SPEECH: WORLD ECONOMY

... I attach a rough draft of a passage on the world economy.

2. As we discussed, I should be grateful for any suggestions to sharpen it up. In particular, paragraphs 2 and 3 need some points to show whether figures released since the Autumn Statement bear out the forecast or not.

3. Please could I have any comments by close on Thursday (11th).

APH

A P HUDSON

ps4/8H Pl. take in amendments

~~**AUTUMN STATEMENT DEBATE: DRAFT PASSAGE ON THE WORLD ECONOMY**~~

The World Economy

The outlook for the British economy will, of course, depend on developments in the world economy.

~~2.~~ In the Autumn Statement, I forecast that growth in the major seven industrial countries would average 3 per cent in 1987, slightly faster than this year. ~~Inflation is set to stay low.~~

A

~~HOM~~

~~3.~~ [~~World trade overall may grow a little more slowly in 1987 than it did this year. The OPEC countries are expected to continue to make sharp reductions in their imports, and there may also be some slowing in US import growth.~~] ~~However,~~ And world ~~world~~ trade in manufacturing [which is of particular importance to UK exporters,] is expected to grow much faster ~~in 1987,~~ than it did in 1986. ~~after the pause in the early part of this year.~~

~~Check~~

~~4.~~ One of the main changes in the world economy over the past 15 months has been the relative fall in the value of the dollar following the Plaza Agreement in September of last year. So far, we have seen some of the familiar initial effects of currency realignments - the first part of the so-called "J-Curve" effect. In particular, the value of US imports has gone up, and with it the US current account deficit. Similarly, in dollar ~~value~~ terms, Japanese exports reached record levels in September of this year. But there are now signs that the tide is turning, which tends to confirm my forecast that Japanese growth might be relatively modest next year. The overall outcome will depend on how far the Japanese implement some of the measures under discussion to boost domestic demand.

C

~~5.~~ ~~[Brief paragraph on prospects for the USA and Germany.]~~

B

~~6.~~ One threat to the progress of the world economy in 1987 is protectionism, a threat which is greater following the recent elections in the United States. This would be a disastrous step backwards. A major step towards freer trade was taken in Uruguay in September, with the agreement on a new GATT round, to include services and agriculture for the first time. I took the initiative in putting the thorny issue of agricultural subsidies on the agenda for the next round of international meetings. And as far as the United States is concerned, the exchange rate fall which they sought at Plaza, to make their industry more competitive, has now taken place.

7. My hope is therefore that countries will continue to co-operate to make world trade more, rather than less, free.

8. The past year or so has seen substantial changes and discontinuities - the halving of the oil price, falls in other commodity prices, and the realignment of exchange rates. And the world economy has ~~come through~~ adjusted, with merely a pause in the growth of world trade. In part at least, this is because the major countries have cooperated in pursuing soundly based policies. ~~It~~ is crucial that ~~in 1987~~ we do not lose our way through failures of policy, such as a retreat into protectionism.

The outlook for 1987 is for faster growth, and it

MR 4/47

CONFIDENTIAL

PWP

FROM: A.P. HUDSON
DATE: 10 December 1986

MR PERETZ

cc: PS/Chief Secretary
Sir P Middleton
Sir T Burns
Mr Cassell
Mr Scholar
Mr Turnbull
Mr H P Evans o/r
Mrs Lomax
Mr Sedgwick
Mr Moore
Mr Culpin
Miss O'Mara
Mr Allan
Mr McIntyre
Mr Dolphin
Mr Cropper
Mr Tyrie
Mr Ross Goobey
Mr Neilson
Miss C. Evans

CHANCELLOR'S AUTUMN STATEMENT DEBATE SPEECH

I attach an outline of the Chancellor's Speech.

2. I have already asked for contributions from you and a number of copy recipients. We have to put a consolidated draft to the Chancellor by the weekend, so I would be grateful for material by close tomorrow if at all possible.

3. I should also be grateful to know if anybody has any new figures or indications which would enliven the sections on the economy.

A P HUDSON

MR 4/46

AUTUMN STATEMENT DEBATE: STRUCTURE

Introduction (APH)

TCSC Report suggested lack of continuity of policy. (APH)

But danger of confusion between:

- policy objectives and intermediate targets;
- indicators and instruments. (APH)

Overriding objective has always been reduction of inflation. (APH)

Always had two sides to anti-inflation policy; monetary and fiscal. (APH)

Monetary policy - set out in Lombard Speech. Stress that interest rates have always been an instrument of monetary policy. (Mr Peretz) 750

Fiscal policy - gradual reduction of PSBR. Cover tax cuts issue. (Mr Scholar) 500

Public expenditure - deal with accusation of lack of continuity of policy. (Mr Turnbull) 500

Sum up continuity. (APH)

Retrospective on 1986. If ever there was a year when policy changes might be expected, this was it. But in fact, policy remained consistent. (APH)

Th. Vindication of policy is record of steady growth and low inflation. (APH)

Th. Forecast for 1987, reinforced by statistics since Autumn Statement. (APH)

Prospects inevitably depend on world economy. Explain forecast for 1987. Cover figures released since Autumn Statement - how far they have confirmed or cast doubt on forecast. Possible message: world economy has come through large changes and discontinuities (oil prices, the dollar etc) with only a pause; important not to lose its way now through policy failure, e.g. protectionism. (APH/Mr Dolphin) 600

Other key developments in 1986:

- privatisation and wider share ownership, mainly on BGC, incorporating some news if at all possible; ~~(Mr McIntyre)~~ (APH)

- Big Bang - an "encouraging but stern" message. (Mrs Lomax)

Attack on Labour:

- Kinnock in America

- £28 billion spending

- training levy

- schizophrenia on public spending: criticise Government for "spending spree" but want to spend much more themselves. (Mr Tyrie)

Question for Mr Hattersley: is public spending too high or too low?

006/2982

CONFIDENTIAL

PWP

CHIEF SECRETARY TO THE TREASURY

FROM: JILL RUTTER
DATE: 10 December 1986

MR TURNBULL

cc:
PS/Chancellor
Sir Peter Middleton
Sir Terence Burns
Mr Scholar
Mr Pirie
Mr Culpin
Miss O'Mara
Mr Allan
Mr Tyrie
Mr Ross Goobey

CHIEF SECRETARY'S WIND-UP SPEECH

The Chief Secretary discussed with you, Miss O'Mara, Mr Pirie and Mr Tyrie his requirements for his wind-up speech on the Autumn Statement debate.

2 The Chief Secretary wanted one major theme to be local government. This should include serious material on waste and inefficiency and draw on the Audit Commission's report - as trailed by Mr Banham. The Chief Secretary asked Mr Tyrie and Mr Pirie to collaborate on this.

3 The Chief Secretary said he would like a fairly solid chunk on social security. Could you co-ordinate with Miss Noble.

4 The Chief Secretary asked for chunks on the following three subjects:

i. manufacturing;

ii balance of payments

iii squandering North Sea oil; Miss O'Mara agreed to provide these three pieces.

5 If possible, I would be grateful for contributions to reach this office by 6.00pm on Friday. Please let me know if you see any difficulties (I think that this should only really apply to local authority section).

Jill Rutter 10.12.86

AUTUMN STATEMENT DEBATE 9 Dec 12 noon.

C, CST, PEM, Sir TB, MCS etc.

Content

More time than usual on TCSC Report / Knock down. Choose which aspects.
Certainly: change of policy + use of selective quotation;
monetary policy;
any PEx points come out of TCSC;
ditto Forecast - may not want;
tax cuts - don't take for granted, wind down expectations.

C Done econ. record before. May be do it again.
PEM Missed if don't do it.
C Got record into a single para.

APH Para 6

C Don't want to pick up these.

APH 7.

C Clearly privatisation, + WSO, very gas-orientated. Not EC; charities won't fit in; Big Bang - "encouraging but stern".
Short section on the world scene. Context.
PEM Cd mention protection.
C 20 mins constructive. 5 mins at end bashing Labour: 3 things - £28 bn; training levy; Oppo schizophrenia, ~~PX~~ show "irresponsible spree" but they want to spend more.
pick up CST ~~[illegible]~~ letter to Hattersley
N.B. v. serious issue.
Cd put questions to R Hatt, 2 or 3. Training levy? Schizo? PL to prime backbenchers.
CST ~~Certainly~~ Want one.

C PSBR (ex priv'n) as prop'n of GDP ↓ ~~[illegible]~~ Kink this year, ∵ of oil.
TB Path will then go up.
C CST will do local authorities.
B. Gould will prob wind up.

N.B. AS debate.

RPC Want a retrospective on the year.
AGT Review of Lab's year.
C Will speak on Kinnock in America. Wash Redskins lost first time this season.

✓ MOM Save up some BGC news for the middle, & ask Oppo what their policy is.

C Must have decisive interventions.

A7 Continuity wraps our policies together. Cf Lab disarray.

CHANCELLOR OF THE EXCHEQUER'S OFFICE: MEETING

SUBJECT	AUTUMN STATEMENT DEBATE
DATE AND TIME	TUESDAY 9 DECEMBER - 12.00
VENUE	~~Chancellor's Room,~~ Treasury/No.11/~~Conference Room/House of Commons~~
PAPERS	Minute from Mr Hudson attached
THOSE ATTENDING	CST [Sir P. Middleton] Sir T. Burns Mr Scholar Mr Turnbull Miss O'Mara Mr Culpin Mr Tyrie Mr P. Lilley cc Mr Allan Mr Hudson Mr Ross Goobey

CONFIDENTIAL

FROM: A P HUDSON

DATE: 9 December 1986

PS/CHIEF SECRETARY

cc Sir P Middleton
Sir T Burns
Mr Scholar
Mr Turnbull
Mr Culpin
Miss O'Mara
Mr Allan
Mr Tyrie
Mr Ross Goobey

CHANCELLOR'S AUTUMN STATEMENT DEBATE SPEECH

... I attach the list of questions to be discussed at today's meeting on the Chancellor's speech for the Autumn Statement Debate.

APH

A P HUDSON

C15/020 CONFIDENTIAL

FROM: A P HUDSON
DATE: 5 December 1986

CHANCELLOR

AUTUMN STATEMENT DEBATE SPEECH

1. I think it would be helpful to discuss these questions about your speech for the Autumn Statement debate.

Motion

2. Should the government motion be along the same lines as in 1985 (copy attached)? Yes.

Length

3. You spoke for a total of 30 minutes last year, and 40 minutes in 1984 when there were a lot of interventions. Should we prepare about 25 minutes worth of material this year? Yes.

Content

4. You have already mentioned two things which you would like to include:

(a) a rebuttal of the TCSC report;

(b) a reinforcement of the message about tax cuts.

5. You will presumably also want to say something about the following subjects, and it would be useful to discuss the balance between them.

(a) Monetary Policy

Not an Autumn Statement matter, but was a major feature of the TCSC report.

(b) Fiscal Policy (no PSBR increase; tax cuts off).

(c) Public Expenditure

(d) The Forecast

Particularly, perhaps, the current account

(e) The Economic Record

6. Do you want to pick up any of the other issues raised during your evidence, such as the relationship with local government, or overheating?

7. Do you want to cover any other particular topics? Looking back at the main events of 1986, possibilities include wider share ownership, charities, the Big Bang and the EC Presidency.

8. Do you want to take any particular line in attacking Labour? I am not aware of any fresh ammunition since the last debate. Since you are opening, you could pose some questions to Mr Hattersley about Opposition policies.

9. Is the attached structure about right?

APH

A P HUDSON

AUTUMN STATEMENT DEBATE: STRUCTURE

1. Quotations produced to suggest lack of continuity of policy.

2. But danger of confusion between:

   - policy objectives and intermediate targets;
   - indicators and instruments.

3. Overriding objective has always been reduction of inflation. Record shows success.

4. Always had two sides to anti-inflation policy; fiscal and monetary.

5. Fiscal policy - gradual reduction of PSBR. Cover tax cuts issue.

6. Monetary policy - set out in Lombard Speech. Stress that interest rates have always been an instrument of monetary policy.

7. Success of policy is record of steady growth and low inflation.

8. Forecast for 1987, reinforced by statistics since Autumn Statement.

9. Any particular topics (wider share ownership etc.)

10. Questions to Hattersley.

Autumn Statement 1985-86

4.15 pm

The Chancellor of the Exchequer (Mr. Nigel Lawson): I beg to move,

That this House approves the Autumn Statement presented by Mr. Chancellor of the Exchequer on 12th November; welcomes the prospect of continuing low inflation and steady growth as the basis for maintaining the trend of rising employment; and congratulates Her Majesty's Government on the continuing reduction in the share of national income pre-empted by public expenditure.

Mr. Speaker: I have selected the amendment in the name of the Leader of the Opposition.

Mr. Lawson: Let me start by apologising to the right hon. Member for Birmingham, Sparkbrook (Mr. Hattersley). In our last debate I praised the right hon. Gentleman's writings for *Punch*. I had not realised that this harmless compliment would be used by the SDP to cast doubt on the right hon. Gentleman's working class credentials. Apparently, a Mrs. Shirley Williams declared on television last week:

"You aren't working class Roy — you're a very good writer."

Could I make it clear that we on this side of the House, who do not suffer from these class hang-ups, entirely accept that the right hon. Gentleman is every bit as working class as he feels it necessary to be.

Exactly a month ago today I presented my autumn statement to the House. In it I described a satisfactory outlook for growth, inflation and the current account of the balance of payments. I set out this Government's public expenditure planes for the next three years. In the intervening month inflation has fallen back further, to an annual rate of 5·5 per cent., as I predicted, and last week's figures appear to confirm that the long and seemingly inexorable rise in unemployment has at last come to an end. The whole House will, I know, welcome this.

I have read with interest the report of the Treasury and Civil Service Select Committee. Once again, I congratulate the Committee, under the skilful chairmanship of my right hon. Friend the Member for Worthing (Mr. Higgins) on the speed with which it has been produced.

It is useful to recall what the autumn statement is and what it is not. My predecessor presented the first autumn statement to the House in 1982. It contained then, as it does now, three principal elements. The first is a projection of the Government's expenditure plans. This year I have expanded the information available on public expenditure by providing plans not just for the immediate year ahead but for each of the next three years. The second is a new forecast of economic prospects, as required by the Industry Act. The third is the rates of national insurance contributions for the coming year. That is what the autumn statement is.

It comes at the end of the annual public expenditure round and gives the House an early indication, before publication of the public expenditure White Paper, of the Government's spending plans.

The autumn statement is not and has never been a sneak preview of the budget. It is essentially for this reason that I decided this year not to publish either the so-called estimated fiscal adjustment for 1986-87 or the inevitably highly uncertain revenue forecast from which the fiscal adjustment figure could be conventionally derived. I am genuinely sorry that the Committee has not felt able to endorse this common sense decision. I found its arguments on this point distinctly unpersuasive and we shall simply have to agree to disagree. There will be no fiscal adjustment or revenue forecast published this autumn or any subsequent autumn.

Indeed, there could have been no swifter vindication of the decision not to publish a revenue forecast at the time of the autumn statement than the latest developments in the oil market, following the OPEC meeting in Geneva. The dust has not settled on that yet, and it is too soon to form a view of the likely level of oil prices during the coming year, but, in so far as the prospect now is for a lower oil price than was assumed at the time of the autumn statement, it follows that, other things being equal, tax revenues in 1986-87 will be correspondingly lower and the scope for tax reductions in next year's Budget correspondingly diminished. The House and the country should be in no doubt about that.

While it is possible to conceive of a sudden fall in the oil price so great as to cause serious disruption and dislocation to the entire world economy, I find the prospect as unlikely as it is undesirable. Short of that, there is no threat to the British economy. Even now, at its peak, oil accounts for only 6 per cent. of GDP, and we are a substantial oil consumer as well as a substantial producer. What we stand to lose on the swings, we stand to gain on the roundabouts.

Mr. Dick Douglas (Dunfermline, West): Does the right hon. Gentleman agree that he has missed out the fact that we are also a substantial oil exporter thanks to the fact that we are currently producing as much as the Saudis—*[Interruption.]* I am sorry, but we are producing 2.7 million barrels a day, which is much the same as the Saudis. The Chancellor has access to much more information than I, and I am sure that he will correct me if I am wrong. What does he predict will be the oil price in February and March next year when we are likely to be in great difficulties and his fiscal and budgetary strategy is likely to be in ruins?

Mr. Lawson: I will no more make predictions about the oil price in the spring than I will give a fiscal adjustment for 1986-87.

Government policy in this area remains unchanged. I recall a rather similar state of affairs some three years ago, when I was Secretary of State for Energy. The oil price was weak, and the nervous Nellies, if I may borrow a phrase, were talking about "free fall". OPEC decided to hold its meeting, for the first time, in London — in order, so it was said, to bring pressure to bear on Britain to curb its oil production.

I had the very great pleasure of receiving visits from several eminent OPEC oil Ministers, all of whom wanted us to do just that. I explained how that was impossible and how we in the United Kingdom maintain the freest oil province in the world in which decisions on how much to produce are made not by the Government but by the oil companies. That remains so today, and there is no way round it—not even by the back door.

As it happens, United Kingdom oil production is now at its peak, and from now on is likely to be on a gradually declining path, but there is no way in which the United Kingdom will become a country member of OPEC.

MR 4/47

CONFIDENTIAL

pud

FROM: A P. HUDSON

DATE: 10 December 1986

MR PERETZ

cc: PS/Chief Secretary
Sir P Middleton
Sir T Burns
Mr Cassell
Mr Scholar
Mr Turnbull
Mr H P Evans o/r
Mrs Lomax
Mr Sedgwick
Mr Moore
Mr Culpin
Miss O'Mara
Mr Allan
Mr McIntyre
Mr Dolphin
Mr Cropper
Mr Tyrie
Mr Ross Goobey
Mr Neilson
Miss C. Evans

CHANCELLOR'S AUTUMN STATEMENT DEBATE SPEECH

I attach an outline of the Chancellor's Speech.

2. I have already asked for contributions from you and a number of copy recipients. We have to put a consolidated draft to the Chancellor by the weekend, so I would be grateful for material by close tomorrow if at all possible.

3. I should also be grateful to know if anybody has any new figures or indications which would enliven the sections on the economy.

A P HUDSON

AUTUMN STATEMENT DEBATE: STRUCTURE

Introduction (APH)

TCSC Report suggested lack of continuity of policy. (APH)

But danger of confusion between:

- policy objectives and intermediate targets;
- indicators and instruments. (APH)

Overriding objective has always been reduction of inflation. (APH)

Always had two sides to anti-inflation policy; monetary and fiscal. (APH)

Monetary policy - set out in Lombard Speech. Stress that interest rates have always been an instrument of monetary policy. (Mr Peretz)

Fiscal policy - gradual reduction of PSBR. Cover tax cuts issue. (Mr Scholar)

Public expenditure - deal with accusation of lack of continuity of policy. (Mr Turnbull)

Sum up continuity. (APH)

Retrospective on 1986. If ever there was a year when policy changes might be expected, this was it. But in fact, policy remained consistent. (APH)

Vindication of policy is record of steady growth and low inflation. (APH)

Forecast for 1987, reinforced by statistics since Autumn Statement. (APH)

Prospects inevitably depend on world economy. Explain forecast for 1987. Cover figures released since Autumn Statement - how far they have confirmed or cast doubt on forecast. Possible message: world economy has come through large changes and discontinuities (oil prices, the dollar etc) with only a pause; important not to lose its way now through policy failure, e.g. protectionism. (APH/Mr Dolphin)

Other key developments in 1986:

- privatisation and wider share ownership, mainly on BGC, incorporating some news if at all possible;(Mr McIntyre)

- Big Bang - an "encouraging but stern" message. (Mrs Lomax)

Attack on Labour:

- Kinnock in America

- £28 billion spending

- training levy

- schizophrenia on public spending: criticise Government for "spending spree" but want to spend much more themselves. (Mr Tyrie)

Question for Mr Hattersley: is public spending too high or too low?

CHANCELLOR OF THE EXCHEQUER'S OFFICE: MEETING

SUBJECT	AUTUMN STATEMENT DEBATE
DATE AND TIME	TUESDAY 9 DECEMBER - 12.00
VENUE	~~Chancellor's Room, Treasury~~/No.11/~~Conference Room/House of Commons~~
PAPERS	Minute from Mr Hudson attached
THOSE ATTENDING	CST [Sir P. Middleton] Sir T. Burns Mr Scholar Mr Turnbull Miss O'Mara Mr Culpin Mr Tyrie cc Mr Allan Mr Hudson Mr Ross Goobey.

CONFIDENTIAL

FROM: A P HUDSON

DATE: 9 December 1986

PS/CHIEF SECRETARY

cc Sir P Middleton
Sir T Burns
Mr Scholar
Mr Turnbull
Mr Culpin
Miss O'Mara
Mr Allan
Mr Tyrie
Mr Ross Goobey

CHANCELLOR'S AUTUMN STATEMENT DEBATE SPEECH

... I attach the list of questions to be discussed at today's meeting on the Chancellor's speech for the Autumn Statement Debate.

APH

A P HUDSON

C15/020

CONFIDENTIAL

FROM: A P HUDSON

DATE: 5 December 1986

CHANCELLOR

AUTUMN STATEMENT DEBATE SPEECH

1. I think it would be helpful to discuss these questions about your speech for the Autumn Statement debate.

Motion

2. Should the government motion be along the same lines as in 1985 (copy attached)?

Length

3. You spoke for a total of 30 minutes last year, and 40 minutes in 1984 when there were a lot of interventions. Should we prepare about 25 minutes worth of material this year?

Content

4. You have already mentioned two things which you would like to include:

(a) a rebuttal of the TCSC report; No change Highly selective quotation

(b) a reinforcement of the message about tax cuts. Michael & Andrew Wind down expectations

5. You will presumably also want to say something about the following subjects, and it would be useful to discuss the balance between them.

CONFIDENTIAL

(a) Monetary Policy

Rebut TCSC.

Not an Autumn Statement matter, but was a major feature of the TCSC report.

(b) Fiscal Policy (no PSBR increase; tax cuts off).

(c) Public Expenditure → TCSC.

(d) The Forecast → (?) TCSC

World scene.

Particularly, perhaps, the current account

Protection

(e) The Economic Record single paragraph.

Others growth rates

6. Do you want to pick up any of the ~~other issues raised during your evidence, such as the relationship with local government, or overheating?~~

Gas oriented church privatisation & LSO.

7. Do you want to cover any other particular topics? Looking back at the main events of 1986, possibilities include wider share ownership, ~~charities~~, the Big Bang and the EC ~~Presidency~~.

newsy - encouraging
but stern.

8. Do you want to take any particular line in attacking Labour? I am not aware of any fresh ammunition since the last debate. Since you are opening, you could pose some questions to Mr Hattersley about Opposition policies.

5 mins

£28bn
Tracy Levy
Schizophrenia.

Bernie & Lawn
A hidden agenda

9. Is the attached structure about right?

Irresponsible spend spree
+ great deal more.

Three questions.

Kinnock @
Redskins!

A P HUDSON

APH

C15/021

AUTUMN STATEMENT DEBATE: STRUCTURE

1. Quotations produced to suggest lack of continuity of policy.

2. But danger of confusion between:

   - policy objectives and intermediate targets;
   - indicators and instruments.

3. Overriding objective has always been reduction of inflation. Record shows success.

4. Always had two sides to anti-inflation policy; fiscal and monetary.

5. Fiscal policy - gradual reduction of PSBR. Cover tax cuts issue.

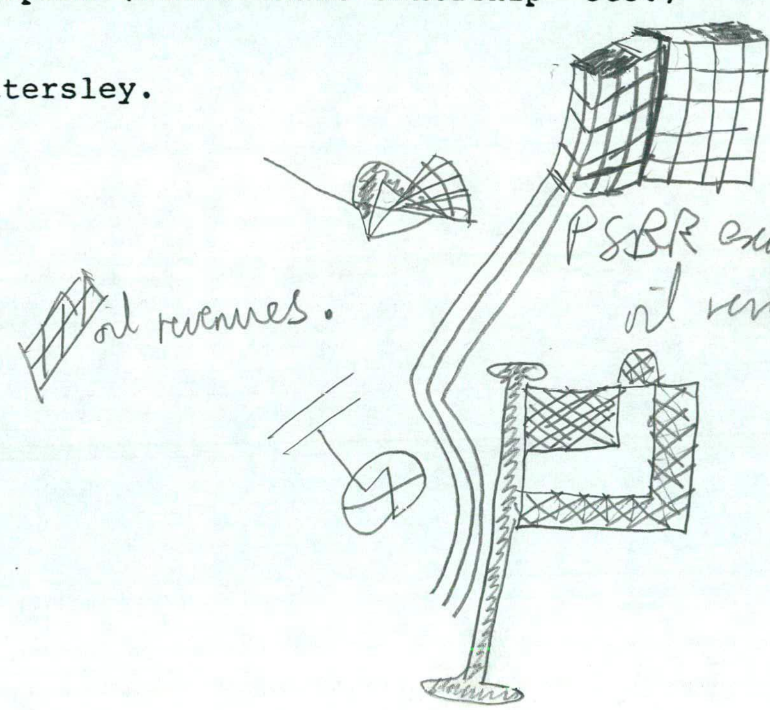
6. Monetary policy - set out in Lombard Speech. Stress that interest rates have always been an instrument of monetary policy.

7. Success of policy is record of steady growth and low inflation.

8. Forecast for 1987, reinforced by statistics since Autumn Statement.

9. Any particular topics (wider share ownership etc.)

10. Questions to Hattersley.



PSBR excludes oil revenues

oil revenues.

Autumn Statement 1985-86

4.15 pm

The Chancellor of the Exchequer (Mr. Nigel Lawson): I beg to move,

That this House approves the Autumn Statement presented by Mr. Chancellor of the Exchequer on 12th November; welcomes the prospect of continuing low inflation and steady growth as the basis for maintaining the trend of rising employment; and congratulates Her Majesty's Government on the continuing reduction in the share of national income pre-empted by public expenditure.

Mr. Speaker: I have selected the amendment in the name of the Leader of the Opposition.

Mr. Lawson: Let me start by apologising to the right hon. Member for Birmingham, Sparkbrook (Mr. Hattersley). In our last debate I praised the right hon. Gentleman's writings for *Punch*. I had not realised that this harmless compliment would be used by the SDP to cast doubt on the right hon. Gentleman's working class credentials. Apparently, a Mrs. Shirley Williams declared on television last week:

"You aren't working class Roy — you're a very good writer."

Could I make it clear that we on this side of the House, who do not suffer from these class hang-ups, entirely accept that the right hon. Gentleman is every bit as working class as he feels it necessary to be.

Exactly a month ago today I presented my autumn statement to the House. In it I described a satisfactory outlook for growth, inflation and the current account of the balance of payments. I set out this Government's public expenditure planes for the next three years. In the intervening month inflation has fallen back further, to an annual rate of 5·5 per cent., as I predicted, and last week's figures appear to confirm that the long and seemingly inexorable rise in unemployment has at last come to an end. The whole House will, I know, welcome this.

I have read with interest the report of the Treasury and Civil Service Select Committee. Once again, I congratulate the Committee, under the skilful chairmanship of my right hon. Friend the Member for Worthing (Mr. Higgins) on the speed with which it has been produced.

It is useful to recall what the autumn statement is and what it is not. My predecessor presented the first autumn statement to the House in 1982. It contained then, as it does now, three principal elements. The first is a projection of the Government's expenditure plans. This year I have expanded the information available on public expenditure by providing plans not just for the immediate year ahead but for each of the next three years. The second is a new forecast of economic prospects, as required by the Industry Act. The third is the rates of national insurance contributions for the coming year. That is what the autumn statement is.

It comes at the end of the annual public expenditure round and gives the House an early indication, before publication of the public expenditure White Paper, of the Government's spending plans.

The autumn statement is not and has never been a sneak preview of the budget. It is essentially for this reason that I decided this year not to publish either the so-called estimated fiscal adjustment for 1986-87 or the inevitably highly uncertain revenue forecast from which the fiscal adjustment figure could be conventionally derived. I am genuinely sorry that the Committee has not felt able to endorse this common sense decision. I found its arguments on this point distinctly unpersuasive and we shall simply have to agree to disagree. There will be no fiscal adjustment or revenue forecast published this autumn or any subsequent autumn.

Indeed, there could have been no swifter vindication of the decision not to publish a revenue forecast at the time of the autumn statement than the latest developments in the oil market, following the OPEC meeting in Geneva. The dust has not settled on that yet, and it is too soon to form a view of the likely level of oil prices during the coming year, but, in so far as the prospect now is for a lower oil price than was assumed at the time of the autumn statement, it follows that, other things being equal, tax revenues in 1986-87 will be correspondingly lower and the scope for tax reductions in next year's Budget correspondingly diminished. The House and the country should be in no doubt about that.

While it is possible to conceive of a sudden fall in the oil price so great as to cause serious disruption and dislocation to the entire world economy, I find the prospect as unlikely as it is undesirable. Short of that, there is no threat to the British economy. Even now, at its peak, oil accounts for only 6 per cent. of GDP, and we are a substantial oil consumer as well as a substantial producer. What we stand to lose on the swings, we stand to gain on the roundabouts.

Mr. Dick Douglas (Dunfermline, West): Does the right hon. Gentleman agree that he has missed out the fact that we are also a substantial oil exporter thanks to the fact that we are currently producing as much as the Saudis— *[Interruption.]* I am sorry, but we are producing 2.7 million barrels a day, which is much the same as the Saudis. The Chancellor has access to much more information than I, and I am sure that he will correct me if I am wrong. What does he predict will be the oil price in February and March next year when we are likely to be in great difficulties and his fiscal and budgetary strategy is likely to be in ruins?

Mr. Lawson: I will no more make predictions about the oil price in the spring than I will give a fiscal adjustment for 1986-87.

Government policy in this area remains unchanged. I recall a rather similar state of affairs some three years ago, when I was Secretary of State for Energy. The oil price was weak, and the nervous Nellies, if I may borrow a phrase, were talking about "free fall". OPEC decided to hold its meeting, for the first time, in London — in order, so it was said, to bring pressure to bear on Britain to curb its oil production.

I had the very great pleasure of receiving visits from several eminent OPEC oil Ministers, all of whom wanted us to do just that. I explained how that was impossible and how we in the United Kingdom maintain the freest oil province in the world in which decisions on how much to produce are made not by the Government but by the oil companies. That remains so today, and there is no way round it—not even by the back door.

As it happens, United Kingdom oil production is now at its peak, and from now on is likely to be on a gradually declining path, but there is no way in which the United Kingdom will become a country member of OPEC.

A+B

PPS Chancellor 12/2

CHANCELLOR - INTERVIEW ON AUTUMN STATEMENT

Transcript from: BBC 1 TV, 9 o'clock News, 6 November 1986

NEWSREADER: The Chancellor, Nigel Lawson, said today that he still wants to cut taxes in the Budget next year. But he warned that higher public spending could reduce the scope for tax cuts. Mr Lawson was speaking during his autumn statement in which he announced an increase in public spending in the year starting next April to £148 billion. That a rise of £4 3/4 billion on the Government's previous plans. Neil Kinnock, the Labour leader, called the increase a strategy to bankroll the Tories for the election but Mr Lawson rejected Labour accusations saying that there'll be no relaxation of the Government's economic strategy.

JAMES LONG: This morning's Cabinet meeting gave the final approval to the Chancellor's spending plans for next year after weeks of negotiation in which Lord Whitelaw's special committee narrowed the gap between what Ministers wanted to spend and what the Treasury would allow. But as Chancellor Nigel Lawson left Downing St to give his speech he knew both sides had had to give ground. The result; he says education is to get an extra £2 1/4, partly for the teacher's pay rise. There's an extra £600 million for health and social care and a further £450 million for housing, some of which will help with council rennovation. The social security budget gets an extra £1 3/4 billion, largely outside the Government's control this and reflecting more people drawing extra benefits. This big rise in spending would seem to cast doubt on scope for tax cuts in the spring but it's combined with a forecast that that the economy will soon start to grow faster. The City's first reaction is that the Chancellor is gambling heavily on that, hoping that companies profits will increase, that people will continue their High St spending spree and that much more tax revenue will come flowing into the Government next year as a result. That way the Chancellor could find there's still room for income tax cuts in the next Budget if it all works out the way he hopes.

JOHN COLE: Christmas is coming and so is the election. Conservative MPs had no doubt after hearing the Chancellor that his new, more relaxed, stance on public spending is the launching pad for their campaign whenever it takes place. Mr Lawson told one disillusioned monetarist that it was wrong to think the Star Chamber which examines spending plans had suddenly turned into a tuck shop. Its chairman, Lord Whitelaw, certainly reckons he's had his toughest round of talks ever. The Chancellor maintains he can afford to spend more because the economy is going well he says. He even hopes unemployment 's going to come down, though he refused to put a date on that. But what about his aim to have an income tax rate of 25 pence ?

CHANCELLOR: I can't tell you where we will be by the time of the next Budget. I have never put a date onto that. It is something which is perfectly realistic, perfectly within our sights. After all we've already gone down from 33 to 29, that's halfway to 25 already.

HATTERSLEY: He'll sacrifice the real long term economic interest if he can get a few votes by cutting taxes before the election in the hope he can win and then make all the painful adjustment afterwards.

ALLIANCE SPOKESMAN: I think the electorate will see through that strategy. I think such a cynical approach to the economy will be condemned by a majority of people in this country. And I think Mr Lawson could easily come a cropper as a result of this U turn.

COLE: So when will the election be? Nobody, including the Prime Minister who decides the date, knows yet. Mrs Thatcher and Lord Whitelaw both think it looks bad to go before the final year of the term for which they've been elected. Now that would point to next autumn or June at the earliest. But one worldly wise young Tory today predicted that the eliction would be on the first April Thursday on which the Government finds itself ahead in the opinion polls. Well that's too rash but the polls have suddenly turned good for the Tories. If they were still ahead next summer and if they did reasonably well in the council elections in May the pressure on Mrs Thatcher to chance her luck might be irresistible. Seeking a third term is always a risky business and hanging on too long leaves more time for banana skins to appear or for the economy to turn sour again.

-----

cc A. B
Mr E.C.R. Butler
Mr Turnbull
Mr Scholar

Rud

CHANCELLOR - INTERVIEW ON AUTUMN STATEMENT

Transcript from: ITN Channel 4, 7 - 8 PM News, 6 November 1986

NEWSREADER: In his autumn statement this afternoon the Chancellor, Nigel Lawson, promised big increases in public spending on health, social security and education. He was also optimistic about growth and jobs but admitted inflation would rise and that the balance of payments would fall into deficit next year. Nick Owen has been speaking to the Chancellor, he asked him why there'd been such a big increase in spending?

CHANCELLOR: Well there are some important increases in expenditure which we have agreed. Reflecting the Government's prioritites a very big increase in expenditure on education, partly of course this is teachers pay but a number of other elements in education including universities. A big increase on the health services too and on the police. So we decided that all these things, they are the Government's priorities, and they shouldhave the money that we can afford within a total public expenditure bill - and it's important to get this clear - within a total public expenditure bill which is a steadily declining share of our total national output, and that we've been managing ~~conistently~~ constantly since 1982.

INTERVIEWER: But you have said that your target is to reduce the basic rate of income tax to 25%, does that remain your target?

CHANCELLOR: Yes it does.

INTERVIEWER: Over what sort of period?

CHANCELLOR: I have never put any particulr date on it because it is always unwise to do so. It depends on the growth of the economy, and the growth of the economy is looking very good at the moment, particularly for the year ahead. It depends on the bouyancy of the revenues. And it depends on the sums that I have to do on the latest forecast I will get at the time of the Budget. But it's impossible to say now.

INTERVIEWER: You talked about a generally encouraging trend in the growth of the economy, your're tallking about growth of 3%, back to 3% next year, but your present forecasts have gone astray haven't they, is there any reason to believe your new estimate will be any more accurate?

CHANCELLOR : Well all forecasts obviously are subject to a margin of error, they're uncertain. But our track record has been pretty good. I mean this year Iforecast 3% it's true and it's turned out now we think 2 1/2%. But that's because it was very difficult this enormous shock of the halving of the oil price, the effect that this would have on the world economy and world trade, it was very difficuult to judge that. But that was exceptional. On the whole our forecasting record has been pretty good and I think that the 3% growth forecast is a pretty reliable one.

INTERVIEWER: But doesn't so much of your forecasting still depend on the behaviour of the oil price which nobody knows where that's going do they?

CHANCELLOR: No, the growth of the economy is not greatly affected by the oil price. It has bearing on tax revenues which is of course one of the reasons why it would be rash to say what the position will be at the time of the Budget. But it does look as if the oil price has settled down now, but not settled down not all that far as it happens from the $15 a barrel which I guessed as the basis for the Budget calculations this March.

INTERVIEWER: Most of these estimates and forecasts, are guesses then are they?

CHANCELLOR: Well the oil price is the only one which I would call a guess because, as you said a moment ago, nobody really knows where the oil price is going to settle down. The others are not guesses but that has an element of guesswork in it and it has proved pretty accurate. And indeed I think most other countries have been making forecasts on the same basis.

INTERVIEWER: You make much of your achievemnts on inflation, youre talking about that going back to just under 4% by the end of next year I think was your figure, is that such an achievement really after all, that's still way above most of our trading competitors isn't it?

CHANCELLOR: It's above some and it's below others. But our aim is clearly to get it down to ultimately to zero. We've got itdown after all to 3%. There is a slight upward movement in the immediate future which I forecasted. But it'll then come ~~dowown~~ down again because of the policies have brought down from what, 28%, 27-28% it was under the Labour Government, now down to 3% and we will get it down further.

INTERVIEWER: Finally people talk about your spending plans being all the evidence of a pre-election boom - is that what is being stoked up?

CHANCELLOR: No, as we were saying a moment ago, it is a pretty steady growth, a little bit lower than planned this year, 2 1/2% makes it lower than envisaged, but a steady 3% next year and public expenditure as a proportion of total national output continuing to decline. It's a responsible policy, it's a prudent policy.

PPS Chancellor
RW

CHANCELLOR - INTERVIEW ON AUTUMN STATEMENT

Transcript from: BBC Radio 4, Today, 7 November 1986

INTERVIEWER: (JOHN SILVERMAN) Two of today's papers headline front page story, 'Spend, Spend, Spend' and two more resurrect that well worn political label 'U turn'. No prizes for guessing that the subject is yesterday's Autumn Statement by the Chancellor Nigel Lawson. Mr Lawson announced that the Government's target for public expenditure next year has been raised by £4 3/4 billion, which is interpreted by many people as the start of the Conservative's attempt to win a third term in office. Well the Chancellor is in our radio car in Whitehall. Mr Lawson, good morning. It's being said of course in many quarters that you've abandoned monetarist restraint, what do you reply to that?

CHANCELLOR: Well of course there's no truth in that whatever. We're continuing a prudent financial policy. As I made absolutely clear, Government borrowing will not rise one penny as a result of the public expenditure plans which I outlined yesterday. And furthermore, if you look at the figures and I shall be publishing them in a chart shortly but the figures' already been announced for anybody to see, the growth in public expenditure which we are now planning over the next 3 years is if anything slightly less that the growth , average growth, of public expenditure during the whole of our time in office so far.

INTERVIEWER: But part of this extra spending is being financed by raiding the reserves if I can put it like that, is that a prudent policy?

CHANCELLOR: Well no it's a complete mistatement of fact. It's a misunderstanding of the position. Every year some of the money which is allocated to the reserve a year previously we then put out to programmes, what you have to look at is total public expenditure which is the total of the programmes plus the reserve. And that is the correct way to look at it and that is what everybody who understands it knows. And, as I say, if you look at that for those figures you find that the total of public expenditure over the next 3 years is planned to rise certainly in real terms but it will still be a declining share of the total national output. And, as I say, the rate of increase will be if anything slightly less that the rate of increase over the whole of our previous period of office.

INTERVIEWER: A lot of people, perhaps especially those who'll benefit most from the extra spending, will wonder why the money wasn't available earlier and why perhaps it's being made available so close to an election?

CHANCELLOR: Well if you'd listened to what I said a moment ago you would have heard me say that in fact there is no increase in the rate of growth of public expenditure. If anything the rate of growth over the next 3 years which we've planned is slightly less than the rate of growth in public expenditure in real terms since we first took office. Therefore your question is based on an entirely false premise.

INTERVIEWER: Nevertheless some spending departments will have money available to spend which perhaps they didn't have some time earlier in this parliament?

CHANCELLOR: Certainly we have shown here where our priorities are and we have allocated important sums of extra money for education, for the health service, for the police, for local authority roads and one or two other areas. But the totality, and I think that is necessary - I think that is sensible - I think that's what people wanted, but the totality of public expenditure as I say is scheduled to rise more slowly than the economy as a whole. In other words it'll be a steadily declining proportion of total national output, as it has been ever since 1982, and the growth in public expenditure in real terms - that's taking away inflation - in real terms will be slightly less if anything than the growth of public expenditure over our period of office to date.

INTERVIEWER: But is it a pure coincidence that those priorities, as you put it, in those areas such as education, health, social security which have been identified as most vulner able for the Conservatives electorally?

CHANCELLOR: Well are you suggesting that we should have spent the money somewhere else, ifso please tell me.

INTERVIEWER: But is the election and the political aspect of this only a minor part of your calculation Mr Lawson?

CHANCELLOR: I have no idea when the general election is going to be. And this has nothing to do with the general election. This is the Government spending money, public money, because public expenditure has always been an important part of the total economy, but we wished it to be a declining part of the total and that is what it is, but using our own priorities to direct money where it can do most good but within an overall prudent financial policy as we've been pursuing up to now, that's why inflation's down to the lowest level for 20 years, and that's what we're continuing to do.

INTERVIEWER: Now does that prudent financial policy still embrace tax cuts, because you said yesterday at one point "clearly a £ cannot be used twice, if it's used for higher public spending it can't be used for reductions in taxation"?

CHANCELLOR: That's absolutely correct. But what the particular prospect will be at the time of the Budget will be revealed at the time of the Budget. And there's no way I can say anything further about the Budget now.

INTERVIEWER: Have you not raised expectations on tax cuts which need to be fulfilled politically?

CHANCELLOR: What I have done is stated very clearly the Government's long term aim in reducing the burden of tax and in particular reducing the burden of income tax. And that's something which distinguishes us from the the other two parties. The other two parties are committed to increasing income tax, we are committed to reducing income tax and getting the basic rate of tax in particular down to 25 pence in the £. But when we shall be able to get there I can't tell you, but get there we shall.

<u>INTERVIEWER:</u> What happens Mr Lawson if the economy doesn't grow as fast you expect it to over the next few months?

<u>CHANCELLOR:</u> That's a purely hypothetical question although our forecasts - I must say it's not just for the next few months - our forecast is for the rest of this year and the whole of 1987.

<u>INTERVIEWER:</u> But if it doesn't grow will this still be seen to be a prudent autumn statement?

<u>CHANCELLOR:</u> It is a prudent autumn statement by any yardstick you care to erect.

- - - -

PPS Chancellor
/ 12/12

071344 :/LAWSON REJECTS CLAIMS BRITAIN HAS CHANGED COURSE A

By Sten Stovall, Reuters

LONDON, Nov 7 - Chancellor of the Exchequer Nigel Lawson today denied he had changed course on economic policy, or that his announcement of big rises in public spending in coming years was designed to win an early election.

But financial and political analysts widely agree that the Conservative government had done, if not a U-turn, then at least a wide swerve on its path towards increased fiscal rectitude.

Analysts said the apparant change in emphasis suggested the Conservatives, emboldened by suddenly taking the lead in recent political opinion polls, may opt for an early election in 1987.

MORE

NNNN
#
CN AA RIM907

071345 :LAWSON REJECTS =2 LONDON

In his Autumn Statement to Parliament on Thursday, Lawson stated that the government was abandoning its struggle to keep public spending roughly constant in inflation-adjusted terms.

In a radio interview today, he acknowledged that public expenditure over the next three years would rise in real terms, but insisted that it will still be a declining share of Britain's total national output.

He said that "the rate of increase will be if anything slightly less than the rate of increase over the whole of our previous period in office."

The ruling Conservative party has been in office since 1979.

MORE

NNNN
#
CN AA RIM908

071347 :LAWSON REJECTS =3 LONDON

Asked whether preparations for a general election had played a role in the government's plans to raise public spending, Lawson replied in the radio interview that "this has nothing to do with the general election. I have no idea when the general election is going to be."

He did stress where the money was going, however.

"We have shown where our priorities are and we have allocated important sums of extra money for education, for the health service, for the police, for local authority roads and one or two other areas."

"I think that's what people wanted," he said.

MORE

071416 :LAWSON REJECTS =4 LONDON
Analysts were suspicious of the message behind Lawson's economic statement, in which he allocated an extra 7.5 billion stg to government spending departments in fiscal 1987/88.
Economist Roger Bootle of Lloyds Merchant Bank Ltd said "The Autumn Statement is clearly fashioned with a view to winning the next general election -- and the argument for an early one looks stronger."
Peter Fellner of James Capel & Co said "The risks taken on the fiscal side suggest that the Chancellor may not wish to subject his arithmetic to the test of time. An election may follow hard on the heels of the budget (next March)."
MORE

071417 :LAWSON REJECTS =5 LONDON
Financial markets gave a mixed response to Lawson"s Autumn statement. Optimism over prospects of continued Conservative rule were tempered by pessimism that the government may not be able to keep its forecast borrowing unchanged, in light of the planned heavy rises in spending and low contingency reserves.
The British government bond market started the day lower.
A major part of the U.K. public sector borrowing requirement (PSBR), targetted at 7.0 billion stg for this year and next, is financed by sales of British government bonds.
Peter Fellner said "we calculate a PSBR next year of maybe as much as nine billion stg, even assuming no tax cuts."
MORE

071434 :LAWSON REJECTS =6 LONDON
Lawson, in his radio interview today with the BBC, would not be drawn on whether next year's budget would include tax cuts.
Asked if prudent financial policy still embraced the government's promises of tax cuts, Lawson confirmed his comment made to parliament yesterday that "clearly a pound sterling cannot be used twice, if that's used for higher public spending it can't be used for reductions in taxation."
He said the Conservative government remained "committed to reducing income tax and getting the basic rate of tax in particular down to 25 pence in the pound." He added, "But when we shall be able to get there I can't tell you."
MORE

071437 :LAWSON REJECTS =7 LONDON
Economist Stephen Lewis of stockbrokers Phillips and Drew said "Lawson has let loose with an election-winning strategy." He added, however, that "The joker in the pack is the pound."
"The Chancellor", Lewis said, "hopes to keep the sterling bears away by convincing markets of a Conservative win at the election. But prudent investors could easily take fright at Britain's rapidly worsening balance of payments deficit and rising inflation."
Lawson forecast a broadly balanced current account for 1986 would slip into a deficit of around 1.5 billion stg next year. Inflation was set to rise to 3.75 pct by 1987's fourth quarter.
MORE

PPS Chancellor PMP
12/2

CHANCELLOR - INTERVIEW ON AUTUMN STATEMENT

Transcript from: : BBC 1 TV, 8 AM News, 7 November 1986

NEWSREADER: AT HOME THE GOVERNMENT HAD A COMFORTABLE MAJORITY OF 164 at the end of last night's Commons debate on the economy. During the debate there were repeated claims by Labour and the Alliance that Chancellor Nigel Lawson's autumn economic statement was an attempt to buy votes if there's an early general election. But Mr Lawson said the £4.7 billion increase in public spending could be achieved within existing borrowing targets. He said there'd been no U turn in the Government's economic policy.

CHANCELLOR: Well it's something we can afford. It's the total amount of expenditure is indeed very large and the increase in education particularly, an increase of £2 1/4 billion over the previous plans is very big indeed and that includes the teachers pay settlement and that is a very big figure in for that. But the revenues are bouyant and we shall have to see what the tax position is when we come to the Budget.

GOULD: The problem for him is this I believe; he either believes what he is doing now, believes that it's right, in which case he's got to explain why it's taken him so so long and why he's put the economy through such a difficult period. He should have the courage and decency to admit that. Or he doesn't believe it, in which case it's straightforward electioneering in the preparation for a consumer boom which he hopes will win the election for him.

ROY JENKINS: What I am slightly sceptical about is making a change and pretending you haven't made a change. And I'm against hypocrisy in these matters. Too much hypocrisy about in politics these days.

-----

i

CHIEF SECRETARY/BRIAN GOULD - INTERVIEWS ON AUTUMN STATEMENT

Transcript from: BBC 1 TV, Good Morning Britain, 7 November 1986

INTERVIEWER: (Frank Bough) Well the Government last night won a substantial victory against Opposition attacks on its AUTUMN economic statement. Labour's leader, Neil Kinnock, accused the Chancellor of trying to as he put it bankroll the Tories for the election. This charge was also made by the SDP Ian Wigglesworth, who attacked the Government for changing course as he said to generate a short term pre-election boom. Demands for more money from Ministers caused the Chancellor to overshoot his original spending targets by £4.75 billion, with the Department of Education getting £2.2 billion, an extra £1.7 billion will be set aside for social security, and £630 million for health and social services and the rest will be used for housing, roads and the police. Well with me now are the Treasury Minister, John Macgregor, and Labour's Treasury spokesman Brian Gould. A very good morning to the pair of you. John you can't blame people for being rather sceptical. One minute there's no money for extra spending, all of a sudden £4.7 billion appear, from where we ask?

CHIEF SEC: Well £4.7 billion appears a lot to a lot of people. But let me put in context. Last year we increased spending after taking account of inflation by just under 1%. This year by just over 1%. And that's because we've had great success with the economy, 6 years of successive economic growth . We are still keeping public spending down as a proportion of our national output which is what we said we'd always do which is necessary for the economy. But what we are able to do is to make judicious and carefully targeted increases in public spending on key areas which we think are priorities because of the success of the economy. So that's what we've done.

INTERVIEWER: There you are Brian Gould.

CHIEF SEC: And it is not a pre-election spending spree.

INTERVIEWER: We'll come onto that in a second. It is all part of the plan he said?

GOULD: Yes, I'm afraid we take a cynical view of this. Incidentally, John Macgregor keeps saying that they're getting public spending down as a proportion of the gross national product, it's still higher than it was in 1979. So even if they were sticking to their own plans they wouldn't be raising it now and that's why we're cynical. We want to see, we very much welcome all this increased spending on schools and housing and health and so because that's what we think we ought to have had a long time ago. But what we're asking I think and with some reason is if it's right to do it now why have we been put through all this misery up until now. And why does the Chancellor keep on pretending that he's sticking to his plans. I think it's perfectly clear that this is a pre-election boom and one question mark which I think everbody ought to have on their mind is will it last beyond an election?

INTERVIEWER: Well they would say of course that it's right to do it now because they're relying on bouyant taxation, on growth and so on and therefore the money is going to be created?

GOULD: Well I wish they'd accept that argument and embrace it wholeheartedly. That's exactly what we've been pressing for a very long time.

CHIEF SEC: What I would say is in fact Brian's got it wrong. We've actually been spending more in real terms, that's to say after taking account of inflation, in key areas like hospitals, like the health service which has been up very substantially over the last few years, like the road programme and all we're doing is actually just carrying that forward. Now we also have to meet a big bill if we can get agreement on teachers pay in order to put that right. And I think that's what the whole country wants. So what we're actually doing is using the economic growth both to get real growth in the economy and also as I say this modest increase in carefully targeted public expenditure areas. Now Brian of course would just go wild. I mean the Labour Party have been making promises which would devastate the economy, put interest rates up and do a great deal of damage and we are very very sensibly and carefully not doing that.

INTERVIEWER: But we're trying to get to grips with what you're saying. I mean Mr Jenkins accused the Chancellor of hypocrisy on television.

CHIEF SEC: Which I thought was quite wrong, as I made clear to him at the time.

INTERVIEWER: Yes but nevertheless you haven't been very keen on public spending and although you'll say this isn't a Uturn it's a fairly substantial swerve in your policies to say the least isn't it?

CHIEF SEC: I remember doing an interview this time last year with you when I was pointing out that because we are going for value for money in public spending, because we are holding it down compared to what the spending spree people would do there's a general implication that all public spending has been held back. And I remember saying to you last year that in fact last year we were increasing on the hospiti als services, on roads and so on and that's what we're continuing on the right things to spend taxpayers money on.

INTERVIEWER: Now before you fire away about it being a precourser to an election I mean surely if you were in power, any political party in power with an election coming up in the foreseeable future, would be trying to create the right kind of climate of booming Britain in order to win the election so what is wrong with that?

GOULD: Well I think what's wrong with it is it's a temporary measure. We would certainly have been trying to expand the economy. We would have been trying to provide the spending to a greater degree and trying to take advantage, as you rightly say, of the increased economic activity to keep it going.

INTERVIEWER: And trying to do it just before a general election, surely you would?

GOULD: No no no, that's the big difference Frank. We believe in an economic policy which believes and obtains growth and then picks up the fruits of that growth to keep it going.

INTERVIEWER: But that's what he's said he's doing?

GOULD: No no no, what they've done I think, and it's perfectly clear, is that they've held the brakes on the economy for the reasons of monetarist discipline and so on which they still say they're sticking to but they've now completely abanboned. Now what they've done therefore is to produce a short term boost to the economy and what I fear and what I think the people of this country ought to fear is that if they were to re-elect a Tory Government the brakes wou ld be slammed on straightaway as soon as ...

CHIEF SEC: That's absolutely wrong actually. We've had economic growth steadily of 3% a year for the last 6, which has been greater than there was throughoust the whole of the Labour Government.

GOULD: Not this year, your forecast is wrong.

CHIEF SEC: Slightly down this year but back upagain next year, 3 1/2%.

INTERVIEWER: But if you were wrong last year why should you be right this year?

CHIEF SEC: A tiny difference Frank and there are always these tiny differences. Average growth is about 3% which is certainly a good deal more than we got under the Labour Government and that's what we've been able to achieve and we've done it by this sensible plannning of the economy. Now can I give an example, Government borrowing, as the Chancellor made clear yesterday, is not going to be higher this year and we shall stick to it.

GOULD: But we don't understand what it's going to be next year.

CHIEF SEC: That will come through in the Budget statement as it always does but the Chancellor's made it clear that Government borrowing is not up. So that is a clear indicatiion that we are controlling the economy sensibly.

INTERVIEWER: Final point; you can't spend a £ twice he said, so what's going to happen to the tax cuts?

CHIEF SEC: Well have to wait and see what the Chancellor decides to do in the Budget next year

INTERVIEWER: But he's fudged that hasn't he, we don't know whether we're going to get it now or not?

CHIEF SEC: He said exactly the same yesterday as he said this time last year because there are things that can change between now ...

INTERVIEWER: In other words he fudged it yesterday and last year as well?

CHIEF SEC: No not at all. We had to wait until we got to the Budget last year before he could make a judgement as to what it was right to do.

INTERVIEWER: Final word:

GOULD: Well we've been promised these tax cuts every year since the Government came into office. We haven't had them yet. For the ordinary family , indeed for 95% of households the tax bill is now higher than when this Government came into office. My guess is that the Chancellor for political reasons will be bound to produce something next year but that will only be at the cost of great violence to the principles he says he's running the economy to.

PWP

AUTUMN STATEMENT: ORAL STATEMENT

WITH PERMISSION, MR SPEAKER, I SHOULD LIKE TO MAKE A STATEMENT.

CABINET TODAY AGREED THE GOVERNMENT'S PUBLIC EXPENDITURE PLANS FOR THE NEXT THREE YEARS.

IN THE NORMAL COURSE OF EVENTS THAT WOULD BE FOLLOWED BY THE PUBLICATION OF THE PRINTED AUTUMN STATEMENT, ACCOMPANIED BY AN ORAL STATEMENT TO THE HOUSE, NEXT TUESDAY.

FOR OBVIOUS REASONS THAT IS NOT POSSIBLE THIS YEAR.

SO WHILE THE AUTUMN STATEMENT WILL BE PRINTED IN THE NORMAL WAY AND PRESENTED TO PARLIAMENT AS SOON AS THE HOUSE REASSEMBLES NEXT WEDNESDAY, I THOUGHT IT WOULD BE FOR THE CONVENIENCE OF THE HOUSE IF I MADE MY ORAL STATEMENT TODAY.

THIS WILL COVER ALL THREE OF THE KEY ELEMENTS IN THE PRINTED STATEMENT: THE GOVERNMENT'S OUTLINE PUBLIC EXPENDITURE PLANS FOR EACH OF THE NEXT THREE YEARS AND THE EXPECTED OUTTURN FOR THIS YEAR; PROPOSALS FOR NEXT YEAR'S NATIONAL INSURANCE CONTRIBUTIONS; AND THE FORECAST OF THE ECONOMIC PROSPECTS FOR 1987 REQUIRED BY THE 1975 INDUSTRY ACT.

THE FULL TEXT OF THE ECONOMIC FORECAST, TOGETHER WITH THE PUBLIC EXPENDITURE FIGURES AND THE REST OF THE INFORMATION CUSTOMARILY PUBLISHED WITH THIS STATEMENT WILL BE AVAILABLE FROM THE VOTE OFFICE AS SOON AS I HAVE SAT DOWN.
THEY WILL ALSO APPEAR IN THE PRINTED AUTUMN STATEMENT TO BE PUBLISHED NEXT WEEK.

I TURN FIRST TO THE OUTTURN FOR THE CURRENT FINANCIAL YEAR, 1986-87.

THE PUBLIC EXPENDITURE PLANNING TOTAL NOW LOOKS LIKELY TO AMOUNT TO ALMOST £140½ BILLION - £1¼ BILLION, OR A LITTLE LESS THAN 1 PER CENT, ABOVE WHAT WAS ALLOWED FOR IN THIS YEAR'S PUBLIC EXPENDITURE WHITE PAPER.

THE MAIN REASON FOR THIS EXCESS IS A 9 PER CENT RISE IN THE CURRENT SPENDING OF LOCAL AUTHORITIES - FAR MORE THAN WAS PROVIDED FOR.

HOWEVER, OTHER ITEMS ON THE EXPENDITURE SIDE, THE LARGEST OF WHICH IS DEBT INTEREST, ARE LIKELY TO FALL SHORT OF WHAT WAS FORECAST AT THE TIME OF THE BUDGET, THUS REDUCING THE TOTAL OVERRUN ON THE EXPENDITURE SIDE TO ABOUT £½ BILLION.

ON THE RECEIPTS SIDE, THE NORTH SEA TAX TAKE IS LIKELY TO BE EVEN LOWER, BY ABOUT £1 BILLION, THAN I ENVISAGED AT THE TIME OF THE BUDGET, LARGELY BECAUSE FOR A LONG PERIOD THE OIL PRICE HAS BEEN BELOW THE $15 A BARREL LEVEL ON WHICH THE BUDGET ARITHMETIC WAS EXPLICITLY BASED.

THIS SHORTFALL, HOWEVER, IS MORE THAN OFFSET BY THE CONTINUING BUOYANCY OF NON-OIL TAX REVENUES, IN PARTICULAR VAT AND CORPORATION TAX.
NON-OIL REVENUES NOW LOOK LIKELY TO EXCEED THE BUDGET FORECAST BY £2 BILLION.
THIS WOULD IMPLY A NET OVERRUN ON THE RECEIPTS SIDE OF ABOUT £1 BILLION, RATHER MORE THAN THAT ON THE EXPENDITURE SIDE.

BUT THIS WILL BE REDUCED BY A CHANGE I PROPOSE TO MAKE TO THE NORTH SEA FISCAL REGIME.

THE COLLAPSE OF THE OIL PRICE HAS LED TO A SHARP CUTBACK IN INVESTMENT ACTIVITY IN THE NORTH SEA, WITH INEVITABLE CONSEQUENCES FOR THE UK OFFSHORE SUPPLIES INDUSTRY BOTH IN SCOTLAND AND THE NORTH EAST OF ENGLAND.

I THEREFORE PROPOSE, ON A CAREFULLY TARGETED BASIS, TO ACCELERATE THE ARRANGEMENTS FOR THE REPAYMENT TO THE OIL COMPANIES OF ADVANCE PETROLEUM REVENUE TAX DUE TO THEM.

THE DETAILS OF THIS CHANGE, WHICH WILL REQUIRE LEGISLATION EARLY IN THE NEW SESSION OF PARLIAMENT, ARE SET OUT IN A PRESS NOTICE WHICH THE INLAND REVENUE WILL BE ISSUING AS SOON AS I HAVE SAT DOWN.

THE NEW ARRANGEMENTS WILL HAVE A REVENUE COST THIS FINANCIAL YEAR OF SOME £300 MILLION, WHICH WILL BE FULLY RECOUPED OVER THE NEXT THREE YEARS.

TAKING THIS INTO ACCOUNT, THE PUBLIC SECTOR BORROWING REQUIREMENT FOR THE CURRENT YEAR IS STILL FORECAST TO BE ABOUT £7 BILLION, THE FIGURE I SET IN THE BUDGET.

I TURN NOW TO THE PUBLIC EXPENDITURE PLANS FOR THE NEXT THREE YEARS.

SINCE 1982-83, PUBLIC SPENDING, BOTH BEFORE AND AFTER DEDUCTING THE PROCEEDS OF PRIVATISATION, HAS BEEN DECLINING AS A PROPORTION OF NATIONAL OUTPUT.

IT IS SET TO BE LOWER STILL THIS YEAR.

THE GOVERNMENT IS DETERMINED TO ENSURE THAT THIS TREND CONTINUES: TO SEE TO IT THAT TOTAL PUBLIC SPENDING, EVEN WITHOUT TAKING ACCOUNT OF PRIVATISATION PROCEEDS, CONTINUES TO DECLINE AS A PERCENTAGE OF GDP.
THE PLANS I AM ABOUT TO ANNOUNCE FOR THE NEXT THREE YEARS SECURE THAT OBJECTIVE.
INDEED, THEY SHOW THAT BY THE END OF THE PERIOD THE RATIO OF PUBLIC SPENDING TO NATIONAL OUTPUT WILL BE BACK TO THE LEVEL OF THE EARLY SEVENTIES.

BUT WITHIN THIS OVERALL CONSTRAINT, AND IN THE CONTEXT OF ITS POLICY PRIORITIES, THE GOVERNMENT HAS FELT IT RIGHT TO ALLOW AN INCREASE IN THE PREVIOUSLY ANNOUNCED PLANNING TOTALS FOR 1987-88 AND 1988-89.
COMPARED WITH THE PROSPECTIVE OUTTURN FOR THE CURRENT YEAR, WE ARE NOW PLANNING FOR AN AVERAGE GROWTH IN THE PUBLIC EXPENDITURE PLANNING TOTAL OF ABOUT 1¼ PER CENT A YEAR IN REAL TERMS, WELL WITHIN THE PROSPECTIVE GROWTH OF THE ECONOMY AS A WHOLE.

THE NEW PLANNING TOTALS HAVE THUS BEEN SET AT £148½ BILLION FOR 1987-88 AND £154¼ BILLION IN 1988-89, AN INCREASE OF £4¾ BILLION AND £5½ BILLION RESPECTIVELY OVER THE TOTALS PREVIOUSLY PUBLISHED.

FOR 1989-90 THE PLANNING TOTAL HAS BEEN SET AT £161½ BILLION.

AS USUAL, THESE TOTALS INCORPORATE ESTIMATES FOR THE PROCEEDS OF PRIVATISATION.

LAST YEAR I INCREASED THE ESTIMATE OF THESE PROCEEDS VERY SUBSTANTIALLY TO £4¾ BILLION IN EACH OF THE THREE SURVEY YEARS, A FIGURE WHICH I EXPECT TO BE DULY ACHIEVED THIS YEAR.

ALTHOUGH THE PRIVATISATION PROGRAMME IS NOW MOVING AHEAD MORE STRONGLY THAN EVER BEFORE, I HAVE DECIDED TO MAKE ONLY A MODEST FURTHER ADDITION TO THIS ESTIMATE, BRINGING IT TO £5 BILLION IN EACH OF THE NEXT THREE YEARS.

THE NEW PLANNING TOTALS ALSO CONTAIN SUBSTANTIAL

RESERVES, RISING FROM £3½ BILLION IN 1987-88 TO £7½ BILLION IN 1989-90.

THE PUBLIC EXPENDITURE INCREASES I HAVE ANNOUNCED ALLOW US TO MAKE REALISTIC PROVISION BOTH FOR LOCAL AUTHORITY CURRENT EXPENDITURE, OVER WHICH THE GOVERNMENT HAS NO DIRECT CONTROL, AND FOR DEMAND-LED PROGRAMMES SUCH AS SOCIAL SECURITY, WHILE STILL LEAVING SCOPE FOR INCREASED SPENDING ON SERVICES TO WHICH THE GOVERNMENT ATTACHES PARTICULAR PRIORITY.

BUT BEFORE REFERRING TO SOME OF THE MORE IMPORTANT CHANGES, LET ME MAKE ONE THING ABSOLUTELY CLEAR.

THERE CAN BE NO QUESTION OF ALLOWING THE PROJECTED INCREASES IN PUBLIC EXPENDITURE OVER THE NEXT TWO YEARS TO UNDERMINE THE PRUDENCE OF THE GOVERNMENT'S OVERALL FISCAL STANCE.

THE GOVERNMENT'S FISCAL STANCE HAS BEEN CLEARLY SET OUT IN THE MEDIUM-TERM FINANCIAL STRATEGY PUBLISHED AT THE TIME OF THIS YEAR'S BUDGET.

There will be no relaxation of that stance.

Within the totality of public expenditure, the largest increase is for the local authorities, whose current spending next year is now put at £4 billion above the previous provision.

This in part reflects the fact that the previous plans simply carried forward the same level of cash spending as in 1986-87.

At the same time, we are increasing next year's Aggregate Exchequer Grant - the contribution that taxpayers make to local government spending - by almost 10 per cent over this year's Settlement; a rise of almost £1½ billion.

These substantial sums demonstrate in particular the priority the Government is giving to education, which, including the new proposals on pay and conditions of service for teachers announced last week, accounts for about half the increase in provision.

THERE IS ALSO A SUBSTANTIAL INCREASE IN PROVISION FOR THE POLICE.

ON TOP OF THE INCREASED PROVISION FOR THE COST OF EDUCATION IN SCHOOLS, WHICH IS CONTAINED WITHIN LOCAL AUTHORITY CURRENT SPENDING, THERE WILL BE ADDITIONAL SPENDING ON THE UNIVERSITIES OF £60 MILLION IN 1987-88 AND £70 MILLION IN 1988-89.

SPENDING ON THE HEALTH AND PERSONAL SOCIAL SERVICES WILL BE INCREASED BY MORE THAN £600 MILLION.
FOR THE NATIONAL HEALTH SERVICE ALONE, THE INCREASE IN ENGLAND AMOUNTS TO OVER £300 MILLION A YEAR.
COMBINED WITH THE ADDITIONAL RESOURCES BEING GENERATED BY GREATER EFFICIENCY, THIS WILL NOT ONLY ENABLE THE HEALTH SERVICE TO COPE WITH THE GROWING NUMBER OF ELDERLY PATIENTS BUT WILL ALSO ALLOW IT TO IMPROVE SERVICES.

GROSS PROVISION FOR HOUSING INVESTMENT IS BEING INCREASED BY £450 MILLION.

THIS WILL SUSTAIN THE RISING TREND OF SPENDING ON LOCAL AUTHORITY RENOVATION AND IMPROVEMENTS AND PROVIDE ADDITIONAL RESOURCES FOR THE HOUSING ASSOCIATIONS.

IN THE LIGHT OF THIS YEAR'S EXPERIENCE, £1¾ BILLION HAS BEEN ADDED TO NEXT YEAR'S PROVISION FOR SOCIAL SECURITY, MOST OF WHICH REPRESENTS A GREATER EXPECTED EXPENDITURE ON EXISTING MEANS-TESTED BENEFITS.

PROVISION FOR INVESTMENT IN ROADS IS BEING INCREASED BY £65 MILLION NEXT YEAR AND £75 MILLION THE YEAR AFTER, MOSTLY FOR LOCAL AUTHORITY ROADS.

FOR DEFENCE, THE PROVISION REMAINS AS PLANNED IN THE LAST WHITE PAPER AFTER ALLOWING FOR MINOR CHANGES, INCLUDING A REDUCTION IN THE ESTIMATED COST OF THE FALKLANDS DEPLOYMENT.
THE DEFENCE PROGRAMME WILL CONTINUE TO BENEFIT FROM THE SUBSTANTIAL REAL GROWTH IN PREVIOUS YEARS AND THE

WIDE-RANGING ACTION TO IMPROVE EFFICIENCY AND VALUE FOR MONEY.

TAKING ALL PROGRAMMES TOGETHER, THE ADDITIONS TO PLANNED CAPITAL EXPENDITURE AMOUNT TO GETTING ON FOR £1 BILLION IN 1987-88, OF WHICH ABOUT TWO-THIRDS IS LOCAL AUTHORITY SPENDING.

FURTHER DETAILS OF THESE AND OTHER CHANGES WILL BE CONTAINED IN THE PRINTED AUTUMN STATEMENT WHICH WILL BE PUBLISHED AS SOON AS THE HOUSE RETURNS NEXT WEEK. IN ADDITION, FULL DETAILS, TOGETHER WITH INFORMATION ON RUNNING COSTS AND MANPOWER, WILL BE GIVEN IN THE PUBLIC EXPENDITURE WHITE PAPER EARLY IN THE NEW YEAR.

I NOW TURN TO NATIONAL INSURANCE CONTRIBUTIONS.

THE GOVERNMENT HAVE CONDUCTED THE USUAL AUTUMN REVIEW OF CONTRIBUTIONS IN THE LIGHT OF ADVICE FROM THE GOVERNMENT

Actuary on the prospective income and expenditure of the National Insurance Fund, and taking account of the benefit uprating which my Rt Hon Friend the Secretary of State for Social Services announced on 22 October.

The lower earnings limit will be increased next April to £39 a week, in line with the single person's pension, and the upper earnings limit will be similarly raised to £295 a week.

The limits for the reduced rate bands which I announced in last year's Budget will also be increased again in April, but by proportionately larger amounts.
The upper limit for the 5 per cent and 7 per cent bands will be raised to £65 a week and £100 a week respectively, and the upper limit for the 9 per cent rate for employers will be raised to £150 a week.

THE TAXPAYER'S CONTRIBUTION TO THE NATIONAL INSURANCE FUND - THE SO-CALLED TREASURY SUPPLEMENT - WILL BE REDUCED BY 2 PER CENT TO 7 PER CENT, BUT THIS WILL NOT REQUIRE ANY CHANGE IN CONTRIBUTION RATES.
THUS THE MAIN CLASS I CONTRIBUTION RATES WILL ONCE AGAIN REMAIN UNCHANGED AT 9 PER CENT FOR EMPLOYEES AND 10.45 PER CENT FOR EMPLOYERS.

FINALLY, I TURN TO THE INDUSTRY ACT FORECAST.

BOTH GROWTH AND INFLATION HAVE TURNED OUT TO BE SLIGHTLY LOWER THIS YEAR THAN I ENVISAGED AT THE TIME OF THE BUDGET.
GROWTH NOW LOOKS LIKE TURNING OUT AT 2½ PER CENT, AGAINST A BUDGET FORECAST OF 3 PER CENT, AND INFLATION IN THE FOURTH QUARTER OF THIS YEAR IS LIKELY TO BE 3¼ PER CENT, AGAINST THE BUDGET FORECAST OF 3½ PER CENT.

THE PRINCIPAL REASON FOR THIS SLOWER GROWTH HAS BEEN THE DISAPPOINTING PERFORMANCE OF EXPORTS, WHICH WERE HARD HIT BY THE CUTBACK IN SPENDING BY OPEC AND OTHER PRIMARY PRODUCERS AFFECTED BY THE SHARP FALL IN COMMODITY PRICES IN GENERAL AND THE OIL PRICE IN PARTICULAR.

COMBINED WITH A HALVING IN THE VALUE OF OUR OWN OIL EXPORTS, THIS HAS MEANT A SIGNIFICANT DETERIORATION IN THE CURRENT ACCOUNT OF THE BALANCE OF PAYMENTS, FROM A SURPLUS OF SOME £3½ BILLION IN 1985 - AND A CUMULATIVE SURPLUS OF £21 BILLION OVER THE SIX YEARS FROM 1980 TO 1985 INCLUSIVE - TO A FORECAST OF BROAD BALANCE FOR 1986.

LOOKING AHEAD TO 1987 THE PROSPECTS ARE GENERALLY ENCOURAGING.

WHILE THE NECESSARY ADJUSTMENT OF THE EXCHANGE RATE TO THE OIL PRICE COLLAPSE HAS NOW TAKEN PLACE, IT WILL INEVITABLY TAKE TIME BEFORE THE FULL BENEFITS COME

THROUGH IN HIGHER NON-OIL EXPORTS AND LOWER IMPORT GROWTH.

THIS MEANS WE CAN EXPECT THE CURRENT ACCOUNT OF THE BALANCE OF PAYMENTS TO GO INTO DEFICIT NEXT YEAR, FOR THE FIRST TIME SINCE 1979, TO THE TUNE OF SOME £1½ BILLION.

EVEN SO, NON-OIL EXPORTS ARE FORECAST TO RISE NEXT YEAR BY 5½ PER CENT, COMPARED WITH AN INCREASE OF ONLY 1 PER CENT THIS YEAR, WITH MANUFACTURING OUTPUT, IN CONSEQUENCE, UP BY 4 PER CENT.

AND WITH DOMESTIC DEMAND CONTINUING TO EXPAND AT THE SAME RATE AS THIS YEAR, THE ECONOMY OVERALL IS LIKELY TO GROW BY A FURTHER 3 PER CENT NEXT YEAR - THE SIXTH SUCCESSIVE YEAR OF STEADY GROWTH AT AN AVERAGE ANNUAL RATE OF ALMOST 3 PER CENT.

RECORDED INFLATION IS LIKELY TO EDGE UP A LITTLE, TO 3¾ PER CENT IN THE FOURTH QUARTER OF 1987.

THIS IS ALMOST ENTIRELY DUE TO THE EFFECT ON THE RPI OF THE TIMING OF MORTGAGE RATE CHANGES.

THE GOVERNMENT'S COMMITMENT TO A MONETARY POLICY THAT WILL SQUEEZE OUT INFLATION REMAINS UNABATED.

MEANWHILE THE LIKELIHOOD OF FASTER GROWTH NEXT YEAR, COMING AT A TIME WHEN UNEMPLOYMENT ALREADY APPEARS TO HAVE STOPPED RISING, SUGGESTS THAT THE PROSPECTS FOR SOME FALL IN UNEMPLOYMENT ARE NOW MORE PROMISING.

BUT THIS PROMISE COULD STILL BE FRUSTRATED BY EXCESSIVE PAY SETTLEMENTS.

MR SPEAKER, THE STRATEGY WE HAVE FOLLOWED SINCE 1979 HAS BROUGHT INFLATION DOWN TO THE LOWEST LEVEL FOR TWO DECADES, COMBINED WITH SUSTAINED GROWTH AND STEADILY RISING LIVING STANDARDS.

THIS IS A COMBINATION THAT HAS ELUDED SUCCESSIVE GOVERNMENTS FOR A GENERATION.

WE HAVE BROUGHT IT ABOUT BY THE DETERMINED PURSUIT OF FREE MARKETS AND SOUND MONEY.

AND THAT IS WHAT WE WILL STICK TO.

1251/38

FROM: A ROSS GOOBEY
DATE: 11 DECEMBER 1986

RWP

MR HUDSON

cc PS/Chief Secretary
Sir P Middleton
Sir T Burns
Mr Cassell
Mr Scholar
Mr Turnbull
Mr Peretz
Mr H Evans-or
Mrs Lomax
Mr Sedgwick
Mr Moore
Mr Culpin
Miss O'Mara
Mr Allan
Mr McIntyre
Mr Dolphin
Mr Neilson
Miss C Evans
Mr Cropper
Mr Tyrie

CHANCELLOR'S AUTUMN STATEMENT DEBATE SPEECH

You asked for possible contributions.

2. Mr McIntyre is checking whether the new night-shift at Jaguar, which is to create 300 jobs, is included in the 1,600 new jobs figure quoted as having been created since privatisation.

3. I have already pointed out the seeming confusion in paragraph 11 of the TCSC Report between interest rates as an "instrument" and a "determinant" of monetary policy. There might be a passage quoting from the 1980 Green Paper eg:

> "No single statistical measure of the money supply can be expected to encapsualte monetary conditions."

> "It is insufficient to rely on one measure alone."

> "The definition may need to be adjusted from time to time as circumstances change ..... in the face of changes in the institutional structure."

4. Table 1 in paragraph 26 has the unique contradiction of including the Chancellor's indicated level of PSBR for 1987/88 (at £7 billion) but Gavyn Davies' estimate of PSFD based on his expectation of a £9¾ billion PSBR (Table 3, Appendix 1, page 28). This is not exactly convincing, or intellectually honest.

5. I think that there could usefully be a passage in the monetary policy section which demonstrates that we are not blind to the build-up in credit or the broad money aggregates. I know it has been said before, but the impression still remains that we are insouciant to their growth however distorted the measures.

6. There remains the real problem of the abandonment of "broadly level in real terms". The overriding target of a reduction in public spending as a proportion of GDP is rightly emphasised, but I cannot see that, however we put it, policy embodied in the Autumn Statement is consistent with "broadly level in real terms". Either we should reinstate that as a long term policy aim, which may be unattractive since it is probably unattainable, or we accept that our ambitions are slightly lower than hitherto. This would certainly not represent a "u-turn" but merely a more realistic appreciation of the likely outturn.

7. The rest of paragraph 53, drafted I notice by Austin Mitchell (see page xxi), is simply untrue and we can remain robust. If we continue to insist that the change over public expenditure is only presentational, I believe it undermines our denial of change on the other factors.

8. I notice in Appendix 5, Table 4, the simulation on the Treasury model of the consequences of merely monetising the extra expenditure are for, year 4, a current account balance over £3 billion worse, a £3.1 billion higher PSBR and inflation 4.1% higher with the positive short-term effect on employment already declining. What effect might there be of an extra £28 billion is the obvious question.

9. Drawing attention to the invisibles revision (second version!) will undermine a lot of the warnings of Armageddon contained in Bill Martin's evidence, (the most pessimistic). He states (before

the benefit of the revisions) that the invisible estimate for 1986 and 1987 "looks particularly optimistic". His desire to see a 3% annual deregulation over 1987/1988 plus nearly £8 billion of tax increases looks an absurdly alarmist attempt to solve a problem which does not obviously exist.

ARG

A ROSS GOOBEY

4-7a

PWP

FROM: M C SCHOLAR
DATE: 11 DECEMBER 1986

MR HUDSON

cc Sir Peter Middleton
Sir Terence Burns
Mr Odling-Smee
Mr Sedgwick
Mr Turnbull
Mr Culpin
Miss O'Mara
Miss Evans

AUTUMN STATEMENT DEBATE

... I attach a draft of the section on fiscal policy. This follows the Chancellor's specification this afternoon, playing back the Committee's own words ("obscure" and not "coherent") against their Report. It could probably do with some shortening.

2. If copy recipients have any comments please may I have them by 3pm? I will then let you have a revised version.

3. We (Miss Evans and I) are looking for evidence of inconsistency between different Reports by the Committee, as requested.

MCS

M C SCHOLAR

Fiscal policy

The Committee's observations on fiscal policy are, I am afraid, scarcely more coherent. Their complaint here is not that the government's policy has changed, but rather that it is the same. Specifically, they are unhappy that the Autumn Statement reaffirmed the Government's commitment to the same fiscal stance as was set out in the 1986 MTFS.

The reasoning in this part of the Report is, Mr Speaker, frankly obscure. The Committee, spurred on no doubt by their advisers, have decided after all these years to abandon the PSBR as the ~~their preferred~~ measure of fiscal stance, ~~just as~~ So, too, they they seem to want - perversely, given all they have said in the past on the subject - to ignore general government expenditure as ~~a~~ the most comprehensive measure of public expenditure, in favour of the planning total. No reasons are given for this change of mind on their part, other than the assertion that the PSBR can be measured inclusive or exclusive of asset sales - though this is hardly a surprise, ~~this - and~~ that the public sector financial deficit is - I quote - a more "relevant and useful figure". It is a pity that when the Report goes on to give its own estimate of the PSFD for 1987-88 it gives a wholly irrelevant and useless figure - of £14.5 billion, which can in no way be reconciled with the £7 billion figure in the same table for the PSBR for that year.

? our projection is for £11½ billion

But, important though these details are, they are technical errors in this Report. On the main point, the Committee have, I fear, no advice to offer the House. They question whether the PSBR should be held to

since I myself drew attention to the size of the PSBR excluding privatisation proceeds in the Red Book this year. They then go on to argue

$1\frac{3}{4}$ per cent of GDP next year. But they express no view at all as to what would be the appropriate level at which to set it. On this they are silent.

This deficiency in the Report is perhaps an understandable one. But I find it very hard indeed to understand the justification for the slur which the Committee attempt to cast on the Government's commitment to hold the PSBR next year to $1\frac{3}{4}$ per cent of GDP. The reason given in the Report for this - that any forecast of the PSBR is uncertain and subject to a margin of error - is quite beside the point. No-one doubts for a moment that PSBR forecasts are uncertain. But when the Chancellor of the Exchequer on Budget day sets the borrowing requirement at a particular figure he is not simply making a <u>forecast</u>, and I am astonished that the Committee should so misunderstand the Budgetary process to think that that is what he is doing.

The PSBR figure published on Budget day is, nevertheless, subsequently validated, or not, as the case may be, by events; and this government's record here is a very good one. The November PSBR figures, published this week, show that public sector borrowing is firmly on course, or below, the level set in the Budget. Last year the PSBR undershot the Budget level by more than £1 billion. In 1984-85, excluding coal strike effects, the outturn was ~~within~~ about the same level as the Budget estimate.

As to the level of the PSBR, it is, at an estimated $1\frac{3}{4}$ per cent of GDP this year, low by any reckoning, below the general levels of recent years, and far, far below the excessive levels from 1974 to 1979,

when it averaged nearly 7 per cent of GDP or over £20 billion a year at today's prices. This is the picture whether or not ~~asset sales~~ privatisation proceeds are taken into account and it is the picture laid down in successive versions of the MTFS right back to 1980.

<u>**Tax cuts**</u>

Like other commentators, the Treasury Committee have speculated about what all this means for tax cuts. I decided last year no longer to publish a fiscal adjustment in the Autumn Statement, so as to discourage the pointless and misleading calculations which are always made at this time of year. Subsequent events proved the rightness of that course, but ~~it has not wholly succeeded in its purpose~~ the speculation continues.

~~But~~ Let there be no mistake about this. As I have said repeatedly, a pound used in additional expenditure is a pound which is not available for reductions in taxation, unless borrowing increases. But I have ruled out higher borrowing. The increase in public expenditure which I announced for 1987-88, of £4¾ billion, is a very substantial sum. [~~The Treasury Committee suggest that this increase might not rule out tax cuts <u>if</u> it were offset by higher tax revenues. But that is a very big if.~~]

The House should be in no doubt that ~~the~~ this substantial increase ~~in public spending next year~~ has much diminished any scope there might have been for reductions in taxation. Of course the uncertainties are enormous, as we always see in the period between the Autumn Statement and the Budget. But one point there is no uncertainty, and no shadow of doubt - and that is the Government's resolve to keep

borrowing under control, as it consistently has done since 1979; and and take no risks with inflation.

CE6

AUTUMN STATEMENT DEBATE SPEECH: PSBR AND TAX CUTS

The Government's fiscal policy puts the Treasury Committee in some difficulty. Whereas on monetary policy and on public expenditure they protest that things have changed, on the fiscal side they seem unhappy because the PSBR target has <u>not</u> changed. As I explained in my evidence to the Committee the Government's policy on public sector borrowing has shown the same continuity as our monetary policy [which it supports]. In successive versions of the MTFS my predecessor and I have mapped out a course for the PSBR in which it would gradually diminish as a proportion of GDP. Throughout my time as Chancellor I have stuck to this objective. For the current year the PSBR is on track to meet the Budget forecast of £7 billion, in spite of a fall of £2 billion in North Sea oil revenues. Under this Government the PSBR as a proportion of GDP has fallen to reach [2¼] 1½ per cent last year, the lowest percentage since 1971-72, which compares with an average of nearly 7 per cent under the previous Labour government. The ratio looks set to increase by a fraction to [3] 1¾ per cent this year, a very small increase when set against the fall of almost £7 billion in oil revenues between the two years. Notwithstanding the strength of our record I recognised at the time of the Autumn Statement that the increase in our spending plans might be interpreted as a sign of weakening in our resolve to keep borrowing under firm control. That is why, exceptionally at this time of year, I spelt out explicitly that the PSBR next year will be held to the MTFS figure of 1¾ per cent of GDP. The Committee suggest there is a lack of clarity in our fiscal policy - but as I have said repeatedly the rationale is clear: to set the PSBR at a level which can be comfortably financed in a non-inflationary way and this we will continue to do.

Tax cuts

(A) ~~Along with~~ Like other commentators, the Treasury Committee have speculated about what all this means for tax cuts. I decided last year ~~not~~ no longer to publish a fiscal adjustment in the Autumn Statement, so as ~~not~~ to ~~in an attempt to~~ dis~~en~~courage ~~prevent~~ the pointless and misleading calculations ~~of this kind~~ which are always made at this time of year. Subsequent events proved the rightness of that course, ~~but people continue to indulge in guesswork~~ but it has not wholly succeeded in its purpose. But let there be no

(figures in brackets = excluding privatisation proceeds) mistake about this: ~~delusion on this issue~~. As I have said repeatedly, a pound used in additional expenditure is a pound which is not available for reductions in taxation, unless ~~you are prepared~~ borrowing ~~to~~ increases. ~~borrowing which~~ I have ruled that out. The increase~~s~~ in ~~spending~~ public expenditure which I ~~have~~ announced for 1987-88, of £4 3/4 billion, is ~~and 1988-89 are~~ very substantial sum~~s~~, indeed ~~well in excess of the fiscal adjustment for those years projected in the 1986 MTFS~~. The Treasury Committee suggest that ~~these~~ this increase~~s~~ might not rule out tax cuts if ~~they~~ it were offset by higher tax revenues. But that is a very big if. The uncertainties are enormous, as we ~~saw~~ always see in the ~~very volatile~~ period between the Autumn Statement and the Budget ~~last year. There is no way that anyone can predict now what the position will be at the time of next year's Budget. But there should be no shadow of doubt about~~. But on one point there is no uncertainty, and no shadow of doubt — and that is the Government's resolve to keep borrowing under control, as it consistently has done since 1979; and take no risks with inflation.

SECRET
until after Oral Statement
then UNCLASSIFIED

B2 PUBLIC SECTOR BORROWING: HISTORICAL STATISTICS AND INTERNATIONAL COMPARISONS

[See also Fiscal policy 1986-87 to 1989-90: revenue prospects 1986-87 (Brief B1) and Labour market (C7)]

A PSBR HISTORICAL STATISTICS

Factual

(i)

	PSBR			PSBR excluding privatisation proceeds		PSFD(1)	
	Cash (£ billion)	Real terms (1985-86 prices) (£ billion)	Ratio to GDP (per cent)	Cash (£ billion)	Ratio to GDP (per cent)	Cash (£ billion)	Ratio to GDP (per cent)
1970-71	0.8	4.0	1½	0.8	1½	-0.2	-½
1971-72	1.0	4.5	1¾	1.0	1¾	0.7	1
1972-73	2.4	10.5	3½	2.4	3½	2.0	3
1973-74	4.3	17.5	5¾	4.3	5¾	3.5	4¼
1974-75	8.0	27.0	9	8.0	9	6.0	6¾
1975-76	10.3	27.6	9¼	10.3	9¼	8.1	7¼
1976-77	8.3	19.7	6½	8.3	6½	7.4	5¾
1977-78	5.4	11.2	3½	5.9	4	6.6	4½
1978-79	9.2	17.4	5¼	9.2	5¼	8.5	5
Average 1974-75 to 1978-79	8.2	20.6	6¾	8.3	6¾	7.3	5¾
1979-80	10.0	16.1	4¾	10.4	5	8.2	4
1980-81	12.7	17.2	5½	13.1	5½	11.9	5
1981-82	8.6	10.7	3¼	9.1	3½	5.7	2¼
1982-83	8.9	10.2	3¼	9.3	3¼	8.4	3
1983-84	9.8	10.8	3¼	10.9	3½	12.1	4
1984-85(2)	10.2	10.8	3	12.3	3¾	13.8	4¼
1985-86(2)	5.8	5.8	1½	8.5	2¼	7.8	2¼
Average 1979-80 to 1985-86	9.4	11.7	3½	10.5	3¾	9.7	3½
1986-87 (AS forecast)	7	6¾	1¾	11¾	3	[not published]	

(1) Public Sector Financial Deficit.

(2) If adjusted for coal strike, PSBR and PSFD ratios to GDP roughly 0.9 per cent lower in 1984-85 and 0.3 per cent lower in 1985-86.

WPU

[Mr. Dennis Skinner]

cent., the lowest for some time. That means that the gap between the two is 4 per cent., which suggests that the Chancellor's beloved market—the real monetarists of the world who make money out of interest rates—believes that inflation will gradually come back up to 9 per cent., which is why interest rates are not coming down. What does he intend to do to bring inflation down if those handling the money have no confidence in his policy?

Mr. Lawson: On the contrary, the market has considerable confidence in our policies, in sharp contrast with those of the Labour Government, who had to go cap in hand to the International Monetary Fund.

Unemployment remains too high, but all the signs are that it may now be levelling out. October's fall in the adult seasonally adjusted total was the second in three months and the total employed labour force is estimated to have risen by 18,000 in the second quarter of this year, the first rise for nearly four years. Vacancies are up, short-time working is at its lowest for four years and overtime is picking up strongly.

The roots of this recovery lie in increased confidence, lower interest rates and, above all, low inflation. Like most recoveries, it began with a rise in consumer spending and reduced de-stocking. It is now spreading more widely as investment increases in line with growing profitability and exports seem set to benefit from world recovery. There is no sign of any re-emerging inflationary pressure. Government borrowing is lower in relation to GDP than in most OECD countries. The change to a climate of realism and common sense has pervaded all levels of industry. Expectations have fundamentally changed and the response has been seen in lower pay settlements and higher productivity. All this is good news. That is why there is silence from the Opposition.

It is time that the Opposition recognised that recovery has been going on for two years and shows every sign of continuing. During the general election campaign they chose to deny that there was any recovery and offered an alternative prescription for a very different strategy, which the British people decisively rejected. I can see that that must have been galling for them, but they cannot continue wilfully to reject all the evidence that our strategy is succeeding. They must stop selling Britain short.

Mr. Donald Stewart (Western Isles): How does the Chancellor square his own extremely optimistic forecast with today's report from the National Institute of Economic and Social Research, which forecasts lower growth, higher inflation and more unemployment?

Mr. Lawson: The institute, bless its heart, has a very poor track record in forecasting. It is always a purveyor of doom and gloom. Nevertheless, it has improved slightly. Its comparable forecast a year ago suggested that output would grow by only 1 per cent. this year. At least it has now revised its forecast upwards to 2·25 per cent. Perhaps it will get the right answer in the end.

I shall now deal with taxation and with a point in which I know my right hon. Friend the Member for Worthing (Mr. Higgins), among others, is especially interested. In his Budget statement in March my predecessor was able not only to propose tax reductions for the second consecutive year but to say that there was a prospect of a further small reduction in 1984-85. As the House knows —this has occasioned some comment—in my autumn statement last week I said that the up-to-date fiscal outlook suggested that, if anything, there might be a need for some small net increase in taxation next year. It may be helpful if I described the reasons for the changed prospect.

I shall begin with this year. When the Treasury forecasts were published at the time of the Budget the PSBR outturn for 1982-83 was expected to be about £7·5 billion, allowing for some shortfall between planned and actual public expenditure. As the House will recall, there was actually a surge in public spending at the very end of the year and the outcome was much closer to the overall planning figure. The PSBR for 1982-83 thus turned out to be 1·5 billion higher than the figure published in the Red Book at the time of the Budget.

Any estimate of the extent to which public Departments will underspend on their programmes must be highly uncertain even near the end of a financial year. In forming a judgment about the likely underspend in 1982-83 it seemed sensible at the time to give considerable weight to recent experience, especially that of the financial year 1981-82, in which there was a considerable shortfall. I believe that it is now only prudent to plan on this year's outturn, like last year's, coming much closer to the planning figure.

That is the main reason why, despite the measures that I announced on 7 July, we now expect this year's PSBR to be higher than was expected in March, probably by about £2 billion, as I told the House last week.

Many of the same considerations apply to 1984-85.

Mr. Skinner: Wake up at the back there.

Mr. Lawson: In the public expenditure survey just ended we have done as we said we would and held to the planning total of £126·4 billion for 1984-85, published in the February White Paper. I pay tribute to my right hon. and learned Friend the Chief Secretary for that achievement.

Mr. Skinner: The Chancellor's hon. Friends have all dropped off.

Mr. Lawson: If anyone is tempted to drop off I am sure that the hon. Member for Bolsover (Mr. Skinner) will keep him awake.

I have also thought it right to make no allowance for expenditure shortfall next year, in contrast with the £1·2 billion originally allowed this year, and to keep the contingency reserve at £3 billion as in the White Paper. That, of course, has disappointed some of our critics, who hoped to be able to accuse us of fudging the figures. Partly because of higher borrowing both last year and this, we also expect debt interest to be a little higher next year than was previously envisaged. Together, those two factors more than offset a small upward revision in forecast revenue. That is why, despite the improved growth prospect, the overall fiscal prospect has slightly deteriorated since the last Budget.

Mr. Tim Smith (Beaconsfield): Will my right hon. Friend explain why he considers it necessary for the contingency reserve to be increased from £1·5 billion to £3 billion?

Mr. Lawson: I shall deal with the contingency reserve in a moment. The answer to my hon. Friend's question is

Autumn Statement

Mr. Speaker: I have selected the amendment in the name of the Leader of the Opposition. More than 30 hon. Members are anxious to take part in this debate. I therefore intend, once again, to apply the 10 minute limit on speeches between 7 pm and 8.50 pm. I appeal to Privy Councillors and other hon. Members who are called before 7 pm to bear in mind the interests of their colleagues and to keep their speeches brief.

It would be counter-productive for hon. Members to come to the Chair to ascertain where they stand on my preliminary list. I shall do my best to include in this debate those hon. Members who failed to catch my eye during the economic debate and the debate on the Queen's Speech. I shall give preference to those hon. Members today.

4.40 pm

The Chancellor of the Exchequer (Mr. Nigel Lawson): I beg to move,

That this House approves the Autumn Statement presented by Mr. Chancellor of the Exchequer on 12th November; welcomes the prospect of continuing low inflation and steady growth as the basis for maintaining the trend of rising employment; and congratulates Her Majesty's Government on keeping the public expenditure planning total for 1985-86 within the figure published in the 1984 Public Expenditure White Paper (Cmnd. 9143).

This is the third occasion during the past six weeks on which the House has been able to debate the progress of the economy. I welcome this further opportunity for the House to consider in particular the statement I made on 12 November and to endorse the Government's economic strategy, which has already provided almost four years of steady economic growth with falling inflation and, despite the still lamentably high level of unemployment, a steady growth in the number of people in work since the spring of 1983.

That record owes a great deal to our resolution as a Government in tackling the relentless upward pressure of public expenditure, in reducing the share of national income absorbed by the public sector and in bringing forward resources for more productive use by private enterprise. As the Earl of Stockton in his recent and memorable maiden speech in another place said about slimming the public sector:

"it is very disagreeable . . . But it had to be done and it still has to be done."—[*Official Report, House of Lords,* 13 November 1984; Vol. 457, c. 238.]

Mr. Eric S. Heffer (Liverpool, Walton) *rose*——

Mr. Lawson: Before elaborating on those matters, I should like to pay tribute to the Chairman of the Treasury and Civil Service Committee, my right hon. Friend the Member for Worthing (Mr. Higgins), and to the members of his Committee.

Mr. Heffer: Will the right hon. Gentleman give way?

Mr. Lawson: I shall not give way. The House knows that, I normally give way frequently. Mr. Speaker has said that there is a shortage of time, and I shall, therefore, be a little more parsimonious than I normally am in giving way.

I pay tribute to the Committee for the expedition with which it conducted its inquiry into the autumn statement. I know that my right hon. Friend the Member for Worthing will not take it amiss if I say that I do not find myself 100 per cent.in agreement with every word of the Committee's report. My right hon. Friend would perhaps be surprised, and some members of his Committee might even be disappointed or alarmed if that were not so.

The Treasury and Civil Service Committee can justly claim to have something of a proprietary interest in the autumn statement, because it was in response to an earlier report by its predecessor Committee that my right hon. and learned Friend the Foreign Secretary, when he was Chancellor, presented the first autumn statement to the House in November 1982. This year's autumn statement, like its predecessors, brings together a number of announcements that fall to be made at this time of the year. I know that many hon. Members on both sides of the House recognise that its particular value lies in the fact that it allows the public spending plans for the year ahead to be set in the context of a fresh economic forecast.

We continue to make better progress on inflation than most commentators have expected, and this downward pressure should continue in the coming year. Although the forecast in the autumn statement does not predict much of a change in the inflation rate during the next 12 months, we shall still have achieved a significant period when inflation has been at or below five per cent. That was scarcely imaginable when we first took office a little over five years ago. Now, expectations are adjusting to that much lower rate of inflation, providing the basis for the further progress on inflation that our policies are designed to achieve.

Our policies are designed to achieve something else as well. By having a firm grip on public expenditure, holding it broadly constant in real terms over a period of years, we shall as the economy continues to expand, have progressive scope for reductions in taxation not just for the few, but for the many. We have achieved that already by an increase in tax thresholds well ahead of inflation, and I hope that we shall continue to do so. As I have said to both the House and the Committee, this occurs within a wide margin of uncertainty. The scope of perhaps £1·5 billion of tax reductions in the coming budget——

Ms Clare Short (Birmingham, Ladywood): What about the unemployed? Tax cuts will not help them.

Mr. Lawson: —is something which will be of comfort, as the hon. Lady rightly points out, particularly to the unemployed.

We continue to hear it said that the years since 1981 have been a period of weak recovery. A closer examination of the figures shows that the pace of recovery of output has been far from weak. If growth in 1985 turns out as expected in the autumn statement forecast, the economy will have grown since 1981 by almost 12 per cent. That would more than match the output growth during the previous recovery period from 1975 to 1979. It would also compare particularly well with our competitors overseas. As the House knows, last year we had the highest rate of economic growth within the European Community. According to the Commission's latest estimates, this year, thanks to the coal strike, our rate of growth will be around the average for the Community — no better than that. Next year, however, the Commission expects us once again to be right at the top of the Common Market league table for growth. No doubt, we shall hear in due course from the right hon. Member for Birmingham, Sparkbrook (Mr. Hattersley) that there

A - S - Debate 1985.

Autumn Statement 1985-86

4.15 pm

The Chancellor of the Exchequer (Mr. Nigel Lawson): I beg to move,

That this House approves the Autumn Statement presented by Mr. Chancellor of the Exchequer on 12th November; welcomes the prospect of continuing low inflation and steady growth as the basis for maintaining the trend of rising employment; and congratulates Her Majesty's Government on the continuing reduction in the share of national income pre-empted by public expenditure.

Mr. Speaker: I have selected the amendment in the name of the Leader of the Opposition.

Mr. Lawson: Let me start by apologising to the right hon. Member for Birmingham, Sparkbrook (Mr. Hattersley). In our last debate I praised the right hon. Gentleman's writings for *Punch*. I had not realised that this harmless compliment would be used by the SDP to cast doubt on the right hon. Gentleman's working class credentials. Apparently, a Mrs. Shirley Williams declared on television last week

"You aren't working class Roy — you're a very good writer."

Could I make it clear that we on this side of the House, who do not suffer from these class hang-ups, entirely accept that the right hon. Gentleman is every bit as working class as he feels it necessary to be.

Exactly a month ago today I presented my autumn statement to the House. In it I described a satisfactory outlook for growth, inflation and th current account of the balanhce of payments. I set out this Government's public expenditure planes for the next three years. In the intervening month inflation has fallen back further, to an annual rate of 5½ per cent., as I predicted, and last week's figures appear to confirm that the long and seemingly inexorable rise in unemployment has at last come to an end. The whole House will, I know, welcome this.

I have read with interest the report of the Treasury and Civil Service Select Committee. Once again, I congratulate the Committee, under the skilful chairmanship of my right hon. Friend the Member for Worthing (Mr. Higgins) on the speed with which it has been produced.

It is useful to recall what the autumn statement is and what it is not. My predecessor presented the first autumn statement to the House in 1982. It contained then, as it does now, three principal elements. First, a projection of the Government's expenditure plans. This year I have expanded the information available on public expenditure by providing plans not just for the immediate year ahead but for each of the next three years; secondly a new forecast of economic prospects, as required by the Industry Act; thirdly the rates of national insurance contributions for the coming year. That is what the autumn statement is.

It comes at the end of the annual public expenditure round and gives the House an early indication, before publication of the public expenditure White Paper, of the Government's spending plans.

The autumn statement is not and has never been a sneak preview of the budget. It is essentially for this reason that I decided this year not to publish either the so-called estimated fiscal adjustment for 1986-87 or the inevitably highly uncertain revenue forecast from which the fiscal adjustment figure could be conventionally derived. I am genuinely sorry that the Committee has not felt able to endorse this commonsense decision. I found its arguments on this point distinctly unpersuasive and we shall simply have to agree to disagree. There will be no fiscal adjustment or revenue forecast published this autumn or any subsequent autumn.

Indeed, there could have been no swifter vindication of the decision not to publish a revenue forecast at the time of the autumn statement than the latest developments in the oil market, following the OPEC meeting in Geneva. The dust has not settled on that yet, and it is too soon to form a view of the likely level of oil prices during the coming year, but, in so far as the prospect now is for a lower oil price that was assumed at the time of the autumn statement, it follows that, other things being equal, tax revenues in 1986-87 will be correspondingly lower and the scope for tax reductions in next year's Budget correspondingly diminished. The House and the country should be in no doubt about that?

While it is possible to conceive of a sudden fall in the oil price so great as to cause serious disruption and dislocation to the entire world economy, I find the prospect as unlikely as it is undesirable. Short of that, there is no threat to the British economy. Even now, at its peak, oil accounts for only 6 per cent. of GDP, and we are a substantial oil consumer as well as a substantial producer. What we stand to lose on the swings, we stand to gain on the roundabouts.

Mr. Dick Douglas (Dunfermline, West): Does the right hon. Gentleman agree that he has missed out the fact that we are also a substantial oil exporter thanks to the fact that we are currently producing as much as the Saudis— *[Interruption.]* I am sorry, but we are producing 2.7 million barrels a day, which is made the same as the Saudis. The Chancellor has access to much more information than I, and I am sure that he will correct me if I am wrong. What does he predict will be the oil price in February and March next year when we are likely to be in great difficulties and his fiscal and budgetary strategy is likely to be in ruins?

Mr. Lawson: I will no more make predictions about the oil price in the spring than I will give a fiscal adjustment for 1986-87.

Government policy in this area remains unchanged. I recall a rather similar state of affairs some three years ago, when I was Secretary of State for Energy. The oil price was weak, and the nervous Nellies, if I may borrow a phrase, were talking about "free fall". OPEC decided to hold its meeting, for the first time, in London — in order, so it was said, to bring pressure to bear on Britain to curb its oil production.

I had the very great pleasure of receiving visits from several eminent OPEC oil Ministers, all of whom wanted us to do just that. I explained how that was impossible and how we in the United Kingdom maintain the freest oil province in the world in which decisions on how much to produce are made not by the Government but by the oil companies. That remains so today, and there is no way round it—not even by the back door.

As it happens, United Kingdom oil production is now at its peak, and from now on is likely to be on a gradually declining path, but there is no way in which the United Kingdom will become a country member of OPEC.

I return to fiscal policy. There is one respect in which the Treasury and Civil Service Select Committee could from the state sector to the free enterprise sector should be matched by an increase in spending on public sector capital projects, than that the cost of renationalisation, to which the Labour party is committed, should be offset by an equivalent reduction in spending on public sector capital projects. Is that what the right hon. Gentleman is proposing?

Let me commend to the right hon. Gentleman two recent studies by a source which he should find congenial. Mr. Gavyn Davis, an economic adviser to the last Labour Prime Minister, entitled *Selling the Silver and Other Bogus Arguments* and *More on the Privatisation Debate,* which expose all too cruelly the right hon. Gentleman's confusion on this issue. The plain fact is that privatisation is a policy which is justified on its own merits, is successful and popular, and, at the same time, enables us to bring about a great leap forward in wider share ownership, not least among the employees of the companies concerned. Moreover, we shall continue that policy for many years to come, throughout this Parliament and the next.

Only today, more than 200,000 investors have been allocated shares in Cable and Wireless, and three quarters of that massive public offer have gone to those who applied for up to 1,000 shares. When at the end of the day, some time in the 1990s, the privatisation programme comes to a successful conclusion, with the vast bulk of what was once the state sector of industry safety in the free enterprise sector, it may well be right to permit an offsetting increase in public borrowing. But it will, by then, be an increase from an extremely low level.

Already this year public sector borrowing is likely to be far and away the lowest it has been as a proportion of GDP for 14 years. Indeed, it would still be the lowest for 14 years, even if there had been no privatisation and the proceeds had been replaced by additional borrowing. In short, however one looks at it, the Government's fiscal stance is and will remain prudent. It is hard to imagine a greater contrast with the profligate and irresponsible spending and borrowing plans of the Opposition.

Mr. Skinner: During the past three months I have been puzzled that the Government, who for six years are on record as saying that the Labour party and a future Labour Government would borrow money to get rid of the dole queues eight weeks ago sent the Chancellor of the Exchequer, authorised by the Prime Minister, to the currency markets where he borrowed the biggest sum ever borrowed in one day by any Government since the end of the war. He secured $2·5 billion, not to get rid of dole queues or to save the National Health Service, but to rig the currency markets for Ronald Reagan and to save the pound when there are troubles with OPEC. Is it not a scandal, a cheek and hypocritical to attack us for wanting the borrow money to reduce the dole queues?

Mr. Lawson: The hon. Gentleman refers to the strengthening of the reserves by a $2½ billion floating rate issue. There is an interesting difference between what happened with the Labour Government and what happened with us. The Labour Government had to go on their knees, cap in hand to borrow everything that they could, whereas we asked the market for $2 billion, but as everyone was so anxious to lend us money we accepted $2½ billion, instead. That is a fact.

Whether there will be scope for reductions in taxation in next year's Budget, and if so, by how much, is, for the reasons I have made clear, particularly uncertain at present. But when tax reductions do come, they will come as a result of our continued success in keeping public expenditure under control, and they will be permanent.

The statement that I presented to the House last month shows that the Government intend to achieve cash totals that will keep public spending broadly stable in real terms. Therefore, as the economy grows, public spending will continue to fall as a proportion of national output. By 1988-89 the proportion is planned to be down to 41 per cent. To achieve that reduction will be a major prize. It will represent the lowest proportion since the early 1970s.

The Treasury Select Committee properly sought to probe the realism of the figures. To hold public expenditure broadly flat in real terms is a demanding objective, but as I explained to the Committee, I believe that it is one that we will achieve. A number of specific factors will help.

First, the period of substantial real increases in defence expenditure has now come to an end, although we shall maintain and improve our defence capability through the pursuit of greater efficiency. Secondly, we are now expecting much slower growth in the massive social security programme. Thirdly, the particularly rapid fall in inflation since 1978-79 led to a sharp increase in real terms in the interest payable on Government debt. That phase has also come to an end. Those three factors together account for the lion's share of the increase in Government expenditure which we have seen during the past six years. They will not be generating pressure for further increases during the next three years.

The Treasury Select Committee also seemed to complain about what it saw as a major but unannounced change in the Government's economic policy or monetary policy. It is mistaken on both counts. There has been no major change in the Government's financial strategy. Indeed, its continuity is a great source of strength. The evolution that has occurred in the light of changing circumstances could scarcely have been more clearly enunciated, both in my Budget Speech and in my speech at the Mansion House.

In my Budget speech I said

"significant movements in the exchange rate, whatever their cause, can have a short-term impact on the general price level and on inflationary expectations. This process can acquire a momentum of its own, making sound internal policies harder to implement . . .

That is why I have repeatedly argued that it is necessary to take the exchange rate into account in judging monetary conditions . . .

There can be no doubt about the Government's commitment to maintain monetary conditions that will continue to bring down inflation. Short-term interest rates will be held at the level needed to achieve this".—[*Official Report,* 19 March 1985; Vol. 75, c. 789.]

All that has happened since then is that the Government have demonstrated once again that we mean what we say. Not least by resolutely resisting the blandishments of those who would have us seek some opportunistic window through which to depart from that policy. It remains as firmly in place as ever.

The results are impressive.

Mr. Terence Higgins (Worthing): My right hon. Friend said that he did not expect unanimity from the Select Committee, but our report is unanimous. He also said that we did not express a view on the PSBR, but in paragraph 26 we point out that if the fiscal stance is to

RH12.2 UNCLASSIFIED

PWP

FROM: A P HUDSON
DATE: 11 December 1986

MR McINTYRE

cc Mr Moore
Mr Robson
Mrs Brown
Mr M L Williams
Mr Culpin
Miss O'Mara
Ms Leahy
Mr Neilson
Mr Ross Goobey

CHANCELLOR'S AUTUMN STATEMENT DEBATE SPEECH: PRIVATISATION

... I attach a draft passage on privatisation, mainly about BGC.

2. Please could I have any comments by mid-morning tomorrow.

3. Is there likely to be a peace of news on BGC, which the Chancellor could announce in the speech on 17 December? This would add interest to this particular section.

APH

A P HUDSON

P.S. I have just seen Mr Ross Goobey's minute of today. If the figure for new jobs at Jaguar is good, it would be useful.

APH

AUTUMN STATEMENT DEBATE SPEECH: PRIVATISATION

More and more countries are now pursuing similar policies, not just in terms of broad economic strategy, but of micro economic policies too. A key example is privatisation - a policy which we pioneered, and is now being emulated around the world. This year saw the French embark on a privatisation programme. Any other examples from 1986?]

Our own privatisation programme has taken a major step forward with the sale of British Gas. This has been a triumphant success. Some 5 million people decided to buy shares. Most of them were not seeking to make a quick buck - the offer was widely seen as tightly priced. Rather, they saw shareholding - and British Gas - as a sound and sensible way to invest their savings. This bodes well for future privatisations, and indeed for the health of industry and the economy in general.

There will be enormous benefits from exposing British Gas to the attitudes and pressures of the private sector, and to the disciplines of the capital markets.

- Customers will gain from improved efficiency, with the regulatory regime guarding against excessive cost increases.

- Management will be free to manage.

- And no less than 99 per cent of employees took the chance to buy shares, which sharpens their incentive to succeed.

Even before the Gas sale, the number of shareholders had doubled since 1979. And the flotation of the Trustee Savings Bank Group and the sale of British Gas this year have revealed the massive widespread interest that now exists in investment in equities. As on so many issues, the people who are out of step are the Opposition in this House. So I would like to ask the RHM for Sparkbrook a question which is of interest not only to us in the House, but to the 5 million people who have bought shares in British Gas. In the unlikely event of a Labour Government, what would happen to their shares?

I shall gladly give way.

JB

106/3 plwf

FROM: A M DOLPHIN x6160

DATE: 11 December 1986

MR HUDSON

cc Sir T Burns
Mr Scholar
Mr Evans
Mr Sedgwick
Mr Matthews
Mr Culpin
Miss O'Mara
Mr Ross Goobey

CHANCELLOR'S AUTUMN STATEMENT DEBATE SPEECH: WORLD ECONOMY

I would suggest the following changes to your draft:

Paragraph 2 - Replace the second sentence with:

A

"The latest industrial production figures released by these countries bear out this assessment. Output in the third quarter in France, the United States and of course, the United Kingdom, was up markedly compared with the second quarter. I expect this upward trend to be maintained into 1987. Meanwhile, the annual rate of inflation in the seven Summit countries ~~has remained below 1½ per cent, and it~~ is set to stay low." , as the benefits of lower oil prices feed through.

Paragraph 3 - This causes some problems. It is difficult to get across in such a short section of a speech the reasons underlying the different patterns of growth of overall world trade and trade in manufactures, and perhaps the House of Commons is not the right place for a discourse on the subject. Could we leave this paragraph out? Alternatively, we should stick to something simple along the following lines:

? use 2nd sentence.

"World trade has been disrupted by the fall in oil prices. The OPEC countries have been making sharp reductions in their imports, but the imports of industrial countries have been growing strongly partly because they are building up stocks of oil."

Paragraph 5 - This could read:

B

"Most forecasters expect GNP in the US and Germany to grow by about 3 per cent next year, though domestic demand should grow much faster in Germany than in the US. This pattern of growth ~~will~~ should contribute to reducing the current account imbalance of the two countries."

Paragraph 7 - This is a bit too downbeat. Could we add another reference to low inflation and point out that the benefits of low oil prices in terms of faster growth are still to come?

Tony Dolphin

A M DOLPHIN

4-7a

PWP

FROM: M C SCHOLAR
DATE: 11 DECEMBER 1986

MR HUDSON

cc Sir Peter Middleton
Sir Terence Burns
Mr Odling-Smee
Mr Sedgwick
Mr Turnbull
Mr Culpin
Miss O'Mara
Miss Evans

AUTUMN STATEMENT DEBATE

... I attach a draft of the section on fiscal policy. This follows the Chancellor's specification this afternoon, playing back the Committee's own words ("obscure" and not "coherent") against their Report. It could probably do with some shortening.

2. If copy recipients have any comments please may I have them by 3pm? I will then let you have a revised version.

3. We (Miss Evans and I) are looking for evidence of inconsistency between different Reports by the Committee, as requested.

MCS

M C SCHOLAR

Fiscal policy

The Committee's observations on fiscal policy are, I am afraid, scarcely more coherent. Their complaint here is not that the government's policy has changed, but rather that it is the same. Specifically, they are unhappy that the Autumn Statement reaffirmed the Government's commitment to the same fiscal stance as was set out in the 1986 MTFS.

The reasoning in this part of the Report is, Mr Speaker, frankly obscure. The Committee, spurred on no doubt by their advisers, have decided after all these years to abandon the PSBR as their preferred measure of fiscal stance, just as they seem to want - perversely, given all they have said in the past on the subject - to ignore general government expenditure as a measure of public expenditure, in favour of the planning total. No reasons are given for this change of mind on their part, other than the assertion that the PSBR can be measured inclusive or exclusive of asset sales - hardly a surprise, this - and that the public sector financial deficit is - I quote - a more "relevant and useful figure". It is a pity that when the Report goes on to give its own estimate of the PSFD for 1987-88 it gives a wholly irrelevant and useless figure - of £14.5 billion, which can in no way be reconciled with the £7 billion figure in the same table for the PSBR for that year.

But, important though these details are, they are technical errors in this Report. On the main point, the Committee have, I fear, no advice to offer the House. They question whether the PSBR <u>should</u> be held to

$1\frac{3}{4}$ per cent of GDP next year. But they express no view at all as to what would be the appropriate level at which to set it. On this they are silent.

This deficiency in the Report is perhaps an understandable one. But I find it very hard indeed to understand the justification for the slur which the Committee attempt to cast on the Government's commitment to hold the PSBR next year to $1\frac{3}{4}$ per cent of GDP. The reason given in the Report for this - that any forecast of the PSBR is uncertain and subject to a margin of error - is quite beside the point. No-one doubts for a moment that PSBR forecasts are uncertain. But when the Chancellor of the Exchequer on Budget day sets the borrowing requirement at a particular figure he is not simply making a <u>forecast</u>, and I am astonished that the Committee should so misunderstand the Budgetary process to think that that is what he is doing.

The PSBR figure published on Budget day is, nevertheless, subsequently validated, or not, as the case may be, by events; and this government's record here is a very good one. The November PSBR figures, published this week, show that public sector borrowing is firmly on course, or below, the level set in the Budget. Last year the PSBR undershot the Budget level by more than £1 billion. In 1984-85, excluding coal strike effects, the outturn was ~~within~~ about the same level as the Budget estimate.

As to the level of the PSBR, it is, at an estimated $1\frac{3}{4}$ per cent of GDP this year, low by any reckoning, below the general levels of recent years, and far, far below the excessive levels from 1974 to 1979,

when it averaged nearly 7 per cent of GDP or over £20 billion a year at today's prices. This is the picture whether or not asset sales are taken into account and it is the picture laid down in successive versions of the MTFS right back to 1980.

Tax cuts

Like other commentators, the Treasury Committee have speculated about what all this means for tax cuts. I decided last year no longer to publish a fiscal adjustment in the Autumn Statement, so as to discourage the pointless and misleading calculations which are always made at this time of year. Subsequent events proved the rightness of that course, but it has not wholly succeeded in its purpose.

But let there be no mistake about this. As I have said repeatedly, a pound used in additional expenditure is a pound which is not available for reductions in taxation, unless borrowing increases. I have ruled out higher borrowing. The increase in public expenditure which I announced for 1987-88, of £4¾ billion, is a very substantial sum. The Treasury Committee suggest that this increase might not rule out tax cuts *if* it were offset by higher tax revenues. But that is a very big if.

The House should be in no doubt that the substantial increase in public spending next year has much diminished any scope there might have been for reductions in taxation. Of course the uncertainties are enormous, as we always see in the period between the Autumn Statement and the Budget. But one point there is no uncertainty, and no shadow of doubt - and that is the Government's resolve to keep

borrowing under control, as it consistently has done since 1979; and and take no risks with inflation.

29/3067-2

PLP

FROM: DAVID PERETZ
11 December 1986

MR HUDSON

cc Sir P Middleton
Sir T Burns
Mr Cassell
Mr Scholar
Mr Culpin
Mr Kelly
Mr Grice
Mr Ross Goobey

CHANCELLOR'S AUTUMN STATEMENT DEBATE SPEECH

I attach the draft passage on monetary policy that you commissioned. It is longer than you need, but you asked me to spread myself.

2. You may be able to make use of some of the material in the earlier parts of the speech, which you are drafting.

3. There is, deliberately, nothing on the EMS. But a passage could be fitted in on page 5.

DLP

D L C PERETZ

29/3067

DRAFT

MONETARY POLICY

I review monetary policy in the Budget, and in the annual restatement of the Government's medium term financial strategy. I will be doing so again in a few months' time.

Nevertheless, as seems to have become customary, the report of the Treasury and Civil Service Select Committee on this year's Autumn Statement comments at some length on the conduct of monetary policy. So I trust the House will bear with me if I also spend some time on that subject, even though it has little direct relationship with the content of the Autumn Statement.

Despite a conspicuous lack of recommendations, the theme of the Select Committee's remarks seems to be that there has very recently been a sharp but concealed departure from the policy and objectives followed over the last seven years. And that the Government is being deliberately obscure about how policy is conducted. In this, I suppose, the Committee at least has the merit of consistency. For their previous reports have carried much the same message, year after year. They have been consistently wrong.

I sometimes have harsh things to say about those who write brokers circulars. So let me make amends by quoting, with approval, from one recent circular: the latest Greenwell Montagu Monetary Bulletin contains the following passage:-

> "An historian dispassionately analysing the evidence to date is almost bound to reach the conclusion that Mr Lawson has gone out of his way to explain how monetary policy is being operated in practice, and how it has evolved, probably more so than any previous Chancellor. He should be given credit for it. A lot of evidence is contained in the annual "Red Book" that accompanies each Budget. The original statement of the Medium Term Financial Strategy was in 1980; it has been updated each year since then. An examination of the sequence of updates shows that policy has not chopped and changed ...".

Quite so.

There has been no change in the aim. That remains, as it always has been, to secure steady downward pressure on inflation.

The way that policy is conducted has developed over the years, as the financial world itself has changed. It it has developed in ways that were always foreseen as possibilities.

Time and again I have explained, at length, what the policy is and how it is operated. In the same patient spirit let me deal this afternoon with four specific current misconceptions.

First, it is said that the Government has abandoned monetary policy, because it has accepted that the aggregate £M3 has proved a misleading indicator of monetary conditions.

At the time of the first MTFS, in 1980, not everyone understood our commitment to financial discipline. It was important to keep policy simple. It made sense to set it out in terms of a target for a single aggregate - £M3 - with which the markets were already familiar.

But at the same time, in the 1980 Green Paper on Monetary Control, we made it clear that no one aggregate is by itself a sufficient measure of monetary conditions. And we foresaw that the definition used and choice of target aggregates might need to be adjusted, in the words of the Green Paper: "as circumstances change" and "in the face of long term changes in the institutional structure".

Of course circumstances did change, and the institutional structure did alter, with the result that the behaviour of £M3 became increasingly hard to interpret. For an otherwise scholarly work I am struck by the absence of any reference in the Select Committee's report to experience overseas. For UK experience has been similar to that of the other major countries, most of which - including Germany - have found their monetary targets overshooting this year.

We cannot and do not ignore the continued rapid growth of £M3 and other measures of broad money. But for a long period now this growth has proved consistent with continued firm downward pressure on inflation. So it must be tested continuously against the evidence of other indicators. Principal among these is MO - the broad monetary base - which has proved a reliable indicator, with a stable trend in velocity from year to year. That is why we adopted it as a target aggregate in 1984.

The Select Committee say they are not convinced that MO is a useful indicator of monetary conditions. I suggest they examine the evidence. They imply that all narrow aggregates are misleading because the behaviour of Ml in the early 1970s did not forshadow the subsequent inflation. Had they looked at the behaviour of MO in the early 1970s instead, they would have seen that it did, indeed, warn of coming inflation.

This year MO has remained within its target range. But its acceleration in recent months was an important factor in the decision to raise interest rates in October by 1%.

A second, misconception is that we have switched from a money to an exchange rate target.

Certainly the exchange rate is very important both as a transmission mechanism for monetary policy and an indicator of monetary conditions. In this country, as in the other major economies, it has come to play a more prominent policy role in recent years, as institutional developments have clouded the meaning of the monetary aggregates. But as long ago as 1980 and early 1981 interest rates were reduced because the exchange rate was indicating that conditions were tight, despite a monetary overshoot. The 1982 MTFS explained that (and I quote):-

> "The behaviour of exchange rate can help in the interpretation of monetary conditions, particularly when the different aggregates are known to be distorted ... the Government considers it appropriate to look at the exchange rate in monitoring domestic monetary conditions and in taking decisions about policy."

A third misconception is that policy has changed from control of the money supply to control of interest rates. This is an elementary confusion between the <u>instrument</u> of monetary policy, interest rates; and the effects of that instrument - in the short run the tightness or otherwise of monetary conditions, and in the longer run the rate of inflation.

Again, this was all set out as long ago as 1980, in the Green Paper on Monetary Control, which makes it clear that apart from fiscal policy, interest rates must be the main instrument of monetary policy. And of course fiscal policy is set only once a year, at the time of the Budget.

Fourth, and this is my last point on monetary policy, it is suggested that policy at present is in some way uncertain. It is said that the Government wants both to prevent interest rates from rising and to prevent the exchange rate from falling.

It is true that the operation of policy is complicated. So is the real world. There are difficult judgments to be made. And the timing of decisions on interest rates, is affected by considerations of market tactics. But there is no uncertainty of purpose. Interest rates are and will be set at whatever level, on average, is needed to keep downward pressure on inflation.

Of course no one <u>wants</u> interest rates to be higher than they have to be. But the greatest disservice the Government could do to the economy would be to permit monetary conditions to develop that allowed inflation to take hold again.

The dramatic fall in the price of oil earlier this year meant that some fall in the exchange rate was both necessary and desirable, to help the economy to adjust to a lower oil price. We were able to let the exchange rate fall without a loosening of monetary conditions.

But that was an unusual circumstance. More often a significant fall in the exchange rate is a clear signal of inflationary pressures, requiring policy action, unless there is reassuring evidence from other reliable indicators such as MO. I will certainly not hesitate to raise interest rates again should that be necessary.

005/73

From: A TURNBULL

Date: 11 December 1986

MR A ~~D~~ HUDSON - 13/2nd

cc PS/Chancellor
PS/Chief Secretary
Mr Scholar
Miss O'Mara
Mr Tyrie

CHANCELLOR'S AUTUMN STATEMENT DEBATE SPEECH

I attach a passage on public expenditure for the Chancellor's speech. The paragraph on continuity as it relates to the individual programmes is optional for the Chancellor but I know it is a theme the Chief Secretary would be willing to pick up from the cutting room floor.

2. You suggest that the final question to Mr Hattersley should be whether public spending is too high or too low? I don't think Mr Hattersley would have much difficulty in answering this. His answer was that in aggregate a higher level of public spending can be justified and can be financed. The criticism is two fold.

- this is a government that prides itself on financial control, yet its plans are consistently overshot.
- the pattern of expenditure is wrong. £ billions wasted on social security for the unemployed and on Trident, while essential social services like housing and health are neglected and, equipment for our convential forces is cut.

3. I would go for the confusion over what is or is not in their spending plans.

Ina Perry

pp A TURNBULL

004/73

DRAFT

CHANCELLOR'S AUTUMN STATMENT DEBATE SPEECH

(To follow monetary policy and fiscal policy under broad theme of continuity).

2. By now the Committee's case that there has been "a substantial change in policy" is looking distinctly shaky. The next exhibit is public expenditure. Here, by a textual critique worthy of biblical or Shakespearean scholars, they have sought to find a major change in direction. Which is odd since much of the material at the back of the report is developing the theme that public spending is returning to a trend.

3. In view of this confusion, I ought to clarify the position. First, it has been the long held view of this government that the state takes too much of the nation's income and its share should be reduced. This can be traced back not only to our 1979 manifesto, but even before that to our policy document "The Right Approach to the Economy". We have pursued this objecti~~on~~ve consistently and it has enabled us first to reduce public sector borrowing and in recent budgets to bring down the burden of taxation.

4. It is true that at various points we have set ourselves targets about how fast we would make progress towards this objective, which in the event proved too ambitious. But better demanding targets not fully achieved ~~and~~ than the complete absence of financial discipline offered by the party opposite.

5. The RHG is a literary man and so will be familiar with Browning's Grammarians Funeral.

"That low man goes on adding one to one.

His hundred's soon hit;"

£28 billion actually.

"This high man, aiming at a million,

Misses an unit."

5. If it were indeed the case, as the Committee contend, the policy on public spending has been changed this year, one would expect to be able to detect some break in trend - expenditure rising as a proportion of GDP where it had been falling; or the growth rate accelerating where it had been decelerating.

6. But this is not what one would see. As I explained at the time of my Autumn Statement the rate of increase of public spending in real terms, as measured by the combined spending of central and local government, but as the Committee would wish including debt interest but excluding privatisation proceeds, that rate of increase has been coming down progressively. From 3 per cent in the decade to 1978-79, to 2¼ per cent in the last Parliament and to 1¾ per cent so far in the present one. And our plans, far from reversing that trend to slower growth seek to extend it.

7. Here we are arguing about whether public expenditure will grow by 1 per cent a year, as our plans imply or 1½ per cent a year as suggested by the Committee. Let me remind the House

that the RHG's party increased expenditure in real terms by 12 per cent in a single year.

8. If one looks for a break in trend you will find one certainly, but it was in 1982-83 when the rise in public spending as a proportion of GDP came to an end. In the 4 years since then, the proportion has fallen progressively, and with spending planned to grow significantly more slowly that the economy as a whole, the downward trend will continue, so that by 1989-90, public spending as a proportion of national income will be back to levels last seen in the early 1970s.

9. Some have extended their search for the non-existent U-turn into the detailed programmes themsevles. This search will be equally unproductive. Certainly it is true that additional resources were made available for priority programmes such as education, health and roads. But these are hardly new priorities. Even before the latest Survey spending per pupil in schools was rising in real terms; the real terms increase in the hospitals current budget planned for the current year, 2¼ per cent, is exactly the same as we planned for this year. The roads programme has progressively been restored after the ravages of Labour's panick cuts. Next year, spending on motorways and trunk roads is planned to be 30 per cent up in real terms on 1978-79, compared with the 30 per cent cut under Labour.

10. But let me end on a note of agreement with the Committee. They say at one point in their report that "intended real increases in expenditure may be substantially offset by increases in input

prices". Cutting through the ECO-speak this means that if pay rises too fast jobs and services will be hurt, a message I for one have constantly emphasised. I am delighted therefore to have the Committee's endorsement.

005/73

From: A TURNBULL

Date: 11 December 1986

MR A B HUDSON

Andrew
Some thought
ASe

cc PS/Chancellor — 12/12
PS/Chief Secretary
Mr Scholar
Miss O'Mara
Mr Tyrie

CHANCELLOR'S AUTUMN STATEMENT DEBATE SPEECH

I attach a passage on public expenditure for the Chancellor's speech. The paragraph on continuity as it relates to the individual programmes is optional for the Chancellor but I know it is a theme the Chief Secretary would be willing to pick up from the cutting room floor.

2. You suggest that the final question to Mr Hattersley should be whether public spending is too high or too low? I don't think Mr Hattersley would have much difficulty in answering this. His answer was that in aggregate a higher level of public spending can be justified and can be financed. The criticism is two fold.

- this is a government that prides itself on financial control, yet its plans are consistently overshot.

- the pattern of expenditure is wrong. £ billions wasted on social security for the unemployed and on Trident, while essential social services like housing and health are neglected and, equipment for our convential forces is cut.

3. I would go for the confusion over what is or is not in their spending plans.

Ina Perry

pp A TURNBULL

004/73

DRAFT

CHANCELLOR'S AUTUMN STATMENT DEBATE SPEECH

(To follow monetary policy and fiscal policy under broad theme of continuity).

2. By now the Committee's case that there has been "a substantial change in policy" is looking distinctly shaky. The next exhibit is public expenditure. Here, by a textual critique worthy of biblical or Shakespearean scholars, they have sought to find a major change in direction. Which is odd since much of the material at the back of the report is developing the theme that public spending is returning to a trend.

3. The true position is very simple. ~~In view of this confusion, I ought to clarify the position.~~ First, it has been ~~the~~ our long held view ~~of this government~~ that the state takes too much of the nation's income and its share should be reduced. This can be traced back not only to our 1979 manifesto, but even before that to our policy document "The Right Approach to the Economy". We have pursued this objective consistently and it has enabled us ~~first to reduce public sector borrowing and in recent budgets~~ to bring down the burden of taxation at the same time as reducing public sector borrowing.

X More Annex 2 ?

4. It is true that ~~at various points~~ some of the targets we have set ourselves targets ~~about how fast we would make progress towards this objective, which in the event~~ have proved too ambitious. But it is better to attempt to meet demanding targets ~~not fully achieved and~~ than to have the complete absence of financial discipline offered by the party opposite.

5. The RHG is a literary and a cricketing man and so will be familiar with Browning's Grammarians Funeral.

> "That low man goes on adding one to one.
> His hundred's soon hit;"

£28 billion actually.

> "This high man, aiming at a million,
> Misses an unit."

5. If it were indeed the case, as the Committee contend, that the policy on public spending has been changed this year, one would expect to be able to detect some break in trend - expenditure rising as a proportion of GDP where it had been falling; or the growth rate accelerating where it had been decelerating.

When you look at the figures themselves, such trends are nowhere to be seen.

6. But ~~this is not what one would see~~. As I explained at the time of my Autumn Statement the rate of increase of public spending in real terms ~~as measured by the combined spending of central and local government, but as the Committee would wish including debt interest but~~ even excluding privatisation proceeds, ~~that rate of increase~~ has been coming down progressively. From 3 per cent in the decade to 1978-79, to 2¼ per cent in the last Parliament and to 1¾ per cent so far in the present one. And our plans, far from reversing that trend to slower growth seek to extend it.

GGE needs a separate paragraph

7. Here we are arguing about whether public expenditure will grow by 1 per cent a year, as our plans imply or 1½ per cent a year as suggested by the Committee. Let me remind the House

"Last year the Committee criticised me for focussing on the planning total and so ignoring debt interest. This year I followed their advice and focussed on GGE. ...

that the RHG's party increased expenditure in real terms by 12 per cent in a single year.

8. If one looks for a break in trend you will find one certainly, but it was in 1982-83 when the rise in public spending as a proportion of GDP came to an end. In the 4 years since then, the proportion has fallen progressively, and with spending planned to grow significantly more slowly that the economy as a whole, the downward trend will continue, so that by 1989-90, public spending as a proportion of national income will be back to levels last seen in the early 1970s.

? say why took so long.

9. Some have extended their search for the non-existent U-turn into the detailed programmes themsevles. This search will be equally unproductive. Certainly it is true that additional resources were made available for priority programmes such as education, health and roads. But these are hardly new priorities. Even before the latest Survey spending per pupil in schools was rising in real terms; the real terms increase in the hospitals current budget planned for the current year, 2¼ per cent, is exactly the same as we planned for this year. The roads programme has progressively been restored after the ravages of Labour's panick cuts. Next year, spending on motorways and trunk roads is planned to be 30 per cent up in real terms on 1978-79, compared with the 30 per cent cut under Labour.

10. But let me end on a note of agreement with the Committee. They say at one point in their report that "intended real increases in expenditure may be substantially offset by increases in input

prices". Cutting through the ECO-speak this means that if pay rises too fast jobs and services will be hurt, a message I for one have constantly emphasised. I am delighted therefore to have the Committee's endorsement.

Rws

FROM: D N WALTERS
DATE: 11 DECEMBER 1986

Quite a few lessons for the Budget timetable as well
CE 12.12

1. MISS EVANS
2. MR SCHOLAR

cc PS/Chancellor - 14/2
Mr Sedgwick
Mr Turnbull
Mr Culpin
Mr Davies
Miss O'Mara
Mr Gray
Miss Noble
Mrs Dunn
Mr Short
Mr Pickering
Mr Porteous
Mr Woodall

AUTUMN STATEMENT: POST MORTEM

My minute to Mr Kuczys of 17 November sought views on lessons to be learnt from the mechanics of this year's Autumn Statement exercise. I received nil returns from EA, EB and EOG. The comments of Parliamentary (Mr Savage of 21 November), IDT (Mr Woodall of 21 November), and the Chancellor's Office (Mrs Ryding of 10 November!) are attached. GE are running their own Survey post-mortem but have commented that they were generally happy with the mechanics of the AS exercise.

2. It seems to be generally accepted that the split presentation and the uncertainty surrounding this year's exercise raised particular operational problems which hopefully will not need to be relived in future years. There also seems to be universal acceptance that, thanks to the effort of the staff involved, the whole operation went remarkably smoothly in the prevailing circumstances.

3. Nevertheless, some detailed points have been raised and these, including those set out in my original minute, are summarised below:

Other Departments' Press Notices

4. The arrangements for handling other Departments' Press Notices worked reasonably well and should be retained for future Budget and Autumn Statement exercises. While there was still a last minute

scramble to ensure the arrival of some Press Notices (this will never be completely avoided as some Ministers will always leave clearance of the text until the last moment), the list of telephone contacts and the arrangements made did allow pressure on Departments to be maintained. Nevertheless, valuable suggestions have been made which could improve performance still further:

(a) In future years, we should consider whether those Departments whose spending plans are finalised early on in the Survey should be given an earlier deadline for sending a final version of their Press Notice to the Treasury. This would follow a procedure which we adopted for the last Budget.

(b) While on occasion some departments find it difficult to finalise the text of their Press Notices, the Department of the Environment seem historically to be much the most consistent offender. There is some evidence to suggest that DOE officials just do not get their act together early enough. In future years, we should consider whether it would be worth sending a special letter to Environment pointing out that it is in their interests to see that their Press Notices arrive in good time for inclusion in the Treasury's packages. The Department's message will have much less impact if their Press Notices are not widely available.

(c) To avoid any possible confusion under a tight timetable, it would be helpful to the Chancellor's Office if Departments issuing more than one Press Notice despatched them in separate packages.

Distribution arrangements

5. There was mixed opinion on the clarity, or otherwise, of the distributional annexes to the aide-memoire. However, that some found them less than clear is sufficient reason to note the need to look again at their format for next year's Autumn Statement. In particular, there was some confusion over the arrangements for distribution of packages to outside bodies, eg CBI, NEDC etc. The Chancellor's Office and the Press Office gave different times for collection of packages. At the very least, we should ensure consistency in release times.

6. Other detailed points raised were:

(i) Although the aide-memoire correctly specified the number of packages required by Parliamentary Section, it did not detail who the packages were for. This caused a last minute problem.

(ii) The arrangements should ensure that the Press Officer in the Gallery has additional copies of the oral statement (**only**) to hand out to those journalists who do not have press packs.

Detailed timetabling

7. (i) More precise entries need to be written into the timetable for the handling of the printed document. The spread of the printer's day is not the same as the Treasury's; they generally start and finish earlier. This led to some misunderstanding about when actions would be completed.

(ii) Three important steps in the Parliamentary Branch timetable must be included in future aide-memoires (circumstances allowing):

Day	Event	Action by
Minus one week	Putting on notice the Treasury Spokesman in the House of Lords	Parliamentary Clerk
Minus two days	Letters to the Deliverer of the Vote and Clerk of the Printed Paper Office copied to the House Libraries to establish arrangements for the release of the Oral Statement and associated documents when the Chancellor of the Exchequer sits down	Parliamentary Clerk
by 10.30 am	Official Box List for Statement and Allocation of Gallery Seats to be given to Parliamentary Clerk	APS/Chancellor of the Exchequer

Printing arrangements

8. This year the printer's time was wasted in setting up a first proof of Chapter 1 which was then changed very substantially. Now that we are able to speed up the printing operation by sending discs of the text to HMSO (only charts and tables go as hard copy), we should look in future to strike a better balance between getting a printer's proof early enough for the Chancellor and officials to work on style, layout etc and the need to avoid nugatory work by Macaulay Press. There is probably a good case for cutting out at least one proof stage.

Autumn Statement packages

9. We should be clear at an early date what is to be included in the packages circulated by the Chancellor's Office. This year, copies of the backbenchers' brief were included in the packages for other Cabinet Ministers very much as a last minute thought. Decisions need to be taken earlier. An appropriate entry should be inserted into the timetable.

Miscellaneous

10. On occasions it would have been helpful for officials to have had earlier warning that late evening circulations were envisaged in order for appropriate arrangements for receipt to be made.

Conclusion

11. While, in the circumstances, this year's exercise went remarkably smoothly, all the above point up areas where improvements can still be made. They should all be considered carefully in preparing the timetable for next year's Autumn Statement. The Chancellor's Office will also wish to consider whether any are appropriate for the preparation of this year's Budget aide-memoire.

D N Walters

D N WALTERS

pus

FROM: A P HUDSON
DATE: 11 December 1986

MR McINTYRE

cc ~~Mr Moore~~
Mr Robson 38/1
Mrs Brown
Mr M L Williams
Mr Culpin
Miss O'Mara
Ms Leahy
Mr Neilson
Mr Ross Goobey

CHANCELLOR'S AUTUMN STATEMENT DEBATE SPEECH: PRIVATISATION

... I attach a draft passage on privatisation, mainly about BGC.

2. Please could I have any comments by mid-morning tomorrow.

Y| 3. Is there likely to be a peace of news on BGC, which the Chancellor could announce in the speech on 17 December? This would add interest to this particular section.

APH

A P HUDSON

2000 extra since priv'n

P.S. I have just seen Mr Ross Goobey's minute of today. If the figure for new jobs at Jaguar is good, it would be useful.

APH

Mr Hudson

Two points marked X. I fear the answer on Y is "no".

SAR
12/12

RM14.6

AUTUMN STATEMENT DEBATE SPEECH: PRIVATISATION

More and more countries are now pursuing similar policies, not just in terms of broad economic strategy, but of micro economic policies too. A key example is privatisation - a policy which we pioneered, and is now being emulated around the world. This year saw both the French and the Japanese embark on a privatisation programme. Any other examples from 1986?]

+ Singapore, Brazil, Thailand, W. Germany Canada, Italy, Sweden

Our own privatisation programme has taken a major step forward with the sale of British Gas. This has been a triumphant success. Some 5 million people decided to buy shares. Most of them were not seeking to make a quick buck - the offer was widely seen as tightly priced. Rather, they saw shareholding - and British Gas - as a sound and sensible way to invest their savings. This bodes well for future privatisations, and indeed for the health of industry and the economy in general.

There will be enormous benefits from exposing British Gas to the attitudes and pressures of the private sector, and to the disciplines of the capital markets.

- Customers will gain from improved efficiency, with the regulatory regime guarding against excessive ~~cost~~ price increases.

X

- Management will be free to manage.

- And no less than 9~~0~~5 per cent of employees took the chance to buy shares, which sharpens their incentive to succeed.

Even before the Gas sale, the number of shareholders had doubled since 1979. And the flotation of the Trustee Savings Bank Group and the sale of British Gas this year have revealed the massive widespread interest that now exists in investment in equities. As on so many issues, the people who are out of step are the Opposition in this House. So I would like to ask the RHM for Sparkbrook a question which is of interest not only to us in the House, but to the 5 million people who have bought shares in British Gas. In the unlikely event of a Labour Government, what would happen to their shares?

I shall gladly give way.

4-7a

prg

FROM: M C SCHOLAR
DATE: 11 DECEMBER 1986

MR HUDSON /

cc Sir Peter Middleton
Sir Terence Burns
Mr Odling-Smee
Mr Sedgwick
Mr Turnbull
Mr Culpin
Miss O'Mara
Miss Evans

AUTUMN STATEMENT DEBATE

... I attach a draft of the section on fiscal policy. This follows the Chancellor's specification this afternoon, playing back the Committee's own words ("obscure" and not "coherent") against their Report. It could probably do with some shortening.

2. If copy recipients have any comments please may I have them by 3pm? I will then let you have a revised version.

3. We (Miss Evans and I) are looking for evidence of inconsistency between different Reports by the Committee, as requested.

MCS

M C SCHOLAR

Fiscal policy

The Committee's observations on fiscal policy are, I am afraid, scarcely more coherent. Their complaint here is not that the government's policy has changed, but rather that it is the same. Specifically, they are unhappy that the Autumn Statement reaffirmed the Government's commitment to the same fiscal stance as was set out in the 1986 MTFS.

The reasoning in this part of the Report is, Mr Speaker, frankly obscure. The Committee, spurred on no doubt by their advisers, have decided after all these years to abandon the PSBR as their preferred measure of fiscal stance, just as they seem to want - perversely, given all they have said in the past on the subject - to ignore general government expenditure as a measure of public expenditure, in favour of the planning total. No reasons are given for this change of mind on their part, other than the assertion that the PSBR can be measured inclusive or exclusive of asset sales - hardly a surprise, this - and that the public sector financial deficit is - I quote - a more "relevant and useful figure". It is a pity that when the Report goes on to give its own estimate of the PSFD for 1987-88 it gives a wholly irrelevant and useless figure - of £14.5 billion, which can in no way be reconciled with the £7 billion figure in the same table for the PSBR for that year.

But, important though these details are, they are technical errors in this Report. On the main point, the Committee have, I fear, no advice to offer the House. They question whether the PSBR <u>should</u> be held to

$1\frac{3}{4}$ per cent of GDP next year. But they express no view at all as to what would be the appropriate level at which to set it. On this they are silent.

This deficiency in the Report is perhaps an understandable one. But I find it very hard indeed to understand the justification for the slur which the Committee attempt to cast on the Government's commitment to hold the PSBR next year to $1\frac{3}{4}$ per cent of GDP. The reason given in the Report for this - that any forecast of the PSBR is uncertain and subject to a margin of error - is quite beside the point. No-one doubts for a moment that PSBR forecasts are uncertain. But when the Chancellor of the Exchequer on Budget day sets the borrowing requirement at a particular figure he is not simply making a forecast, and I am astonished that the Committee should so misunderstand the Budgetary process to think that that is what he is doing.

The PSBR figure published on Budget day is, nevertheless, subsequently validated, or not, as the case may be, by events; and this government's record here is a very good one. The November PSBR figures, published this week, show that public sector borrowing is firmly on course, or below, the level set in the Budget. Last year the PSBR undershot the Budget level by more than £1 billion. In 1984-85, excluding coal strike effects, the outturn was within the Budget estimate.

As to the level of the PSBR, it is, at an estimated $1\frac{3}{4}$ per cent of GDP this year, low by any reckoning, below the general levels of recent years, and far, far below the excessive levels from 1974 to 1979,

when it averaged nearly 7 per cent of GDP or over £20 billion a year at today's prices. This is the picture whether or not asset sales are taken into account and it is the picture laid down in successive versions of the MTFS right back to 1980.

Tax cuts

Like other commentators, the Treasury Committee have speculated about what all this means for tax cuts. I decided last year no longer to publish a fiscal adjustment in the Autumn Statement, so as to discourage the pointless and misleading calculations which are always made at this time of year. Subsequent events proved the rightness of that course, but it has not wholly succeeded in its purpose.

But let there be no mistake about this. As I have said repeatedly, a pound used in additional expenditure is a pound which is not available for reductions in taxation, unless borrowing increases. I have ruled out higher borrowing. The increase in public expenditure which I announced for 1987-88, of £4¾ billion, is a very substantial sum. The Treasury Committee suggest that this increase might not rule out tax cuts if it were offset by higher tax revenues. But that is a very big if.

The House should be in no doubt that the substantial increase in public spending next year has much diminished any scope there might have been for reductions in taxation. Of course the uncertainties are enormous, as we always see in the period between the Autumn Statement and the Budget. But one point there is no uncertainty, and no shadow of doubt - and that is the Government's resolve to keep

borrowing under control, as it consistently has done since 1979; and and take no risks with inflation.

1251/38

FROM: A ROSS GOOBEY
DATE: 11 DECEMBER 1986

MR HUDSON

cc PS/Chief Secretary
Sir P Middleton
Sir T Burns
Mr Cassell
Mr Scholar
Mr Turnbull
Mr Peretz
Mr H Evans-or
Mrs Lomax
Mr Sedgwick
Mr Moore
Mr Culpin
Miss O'Mara
Mr Allan
Mr McIntyre
Mr Dolphin
Mr Neilson
Miss C Evans
Mr Cropper
Mr Tyrie

CHANCELLOR'S AUTUMN STATEMENT DEBATE SPEECH

You asked for possible contributions.

2. Mr McIntyre is checking whether the new night-shift at Jaguar, which is to create 300 jobs, is included in the 1,600 new jobs figure quoted as having been created since privatisation.

3. I have already pointed out the seeming confusion in paragraph 11 of the TCSC Report between interest rates as an "instrument" and a "determinant" of monetary policy. There might be a passage quoting from the 1980 Green Paper eg:

> "No single statistical measure of the money supply can be expected to encapsualte monetary conditions."

> "It is insufficient to rely on one measure alone."

> "The definition may need to be adjusted from time to time as circumstances change ..... in the face of changes in the institutional structure."

4. Table 1 in paragraph 26 has the unique contradiction of including the Chancellor's indicated level of PSBR for 1987/88 (at £7 billion) but Gavyn Davies' estimate of PSFD based on his expectation of a £9¾ billion PSBR (Table 3, Appendix 1, page 28). This is not exactly convincing, or intellectually honest.

5. I think that there could usefully be a passage in the monetary policy section which demonstrates that we are not blind to the build-up in credit or the broad money aggregates. I know it has been said before, but the impression still remains that we are insouciant to their growth however distorted the measures.

6. There remains the real problem of the abandonment of "broadly level in real terms". The overriding target of a reduction in public spending as a proportion of GDP is rightly emphasised, but I cannot see that, however we put it, policy embodied in the Autumn Statement is consistent with "broadly level in real terms". Either we should reinstate that as a long term policy aim, which may be unattractive since it is probably unattainable, or we accept that our ambitions are slightly lower than hitherto. This would certainly not represent a "u-turn" but merely a more realistic appreciation of the likely outturn.

7. The rest of paragraph 53, drafted I notice by Austin Mitchell (see page xxi), is simply untrue and we can remain robust. If we continue to insist that the change over public expenditure is only presentational, I believe it undermines our denial of change on the other factors.

8. I notice in Appendix 5, Table 4, the simulation on the Treasury model of the consequences of merely monetising the extra expenditure are for, year 4, a current account balance over £3 billion worse, a £3.1 billion higher PSBR and inflation 4.1% higher with the positive short-term effect on employment already declining. What effect might there be of an extra £28 billion is the obvious question.

9. Drawing attention to the invisibles revision (second version!) will undermine a lot of the warnings of Armageddon contained in Bill Martin's evidence, (the most pessimistic). He states (before

the benefit of the revisions) that the invisible estimate for 1986 and 1987 "looks particularly optimistic". His desire to see a 3% annual deregulation over 1987/1988 plus nearly £8 billion of tax increases looks an absurdly alarmist attempt to solve a problem which does not obviously exist.

ARG

A ROSS GOOBEY

PW

Mr C. W. Kelly   cc Mr Scholar

Mr Allan   Mr Ross Goobey

Miss O'Mara

Mr Culpin

AUTUMN STATEMENT
DEBATE: MONETARY POLICY

Any comments on the attached draft as soon as ~~possp~~ possible, please - it follows closely Mr Peretz's draft.

AHH

12.12.

RM14.4

AUTUMN STATEMENT DEBATE SPEECH: FIRST DRAFT

I beg to move ...

I begin by congratulating the Treasury and the Civil Service Select Committee, under the chairmanship of my RHF the Member for Worthing, on its interesting report on the Autumn Statement, which, as ever, they have produced with commendable promptness.

In the course of my own evidence to the Committee, my RHF the Member for Worthing suggested that the office of Financial Secretary was older than that of Chancellor. That may depend on definitions. But certainly, recent holders of the post of Financial Secretary have achieved distinction in a number of ways. My RHF is Chairman of the Select Committee. The RHM for Ashton-under-Lyne is Chairman of the Public Accounts Committee, and the RHM for Dudley East was recently voted Parliamentarian of the Year.

I have, of course, been privileged to hold both the offices of Financial Secretary and Chancellor, and only one other person has done this - John Herries, who became Chancellor in 1827. Not a household name, but his career is not without interest. In his maiden speech, he opposed the repeal of the window tax. He resigned as

Chancellor after only a few months - over the appointment of a Chairman of the Finance Committee. And later~~, in a statement to the Finance Committee,~~ it was said of him - and I quote -

> "He made the public accounts intelligible, which they never were before."

This is something that I have consistently tried to do, and it is really not fair of the Treasury and Civil Service Committee to suggest otherwise. This Government have been the first to publish the Medium Term Financial Strategy and the first to publish an Autumn Statement. As Chancellor, I have devoted, at a very rough estimate, [ ] words to explaining monetary policy alone. Far from being economical with the truth, I have done my best to explain the truth about the economy. So I was gratified to see this comment in the latest Greenwell Montagu Monetary Bulletin:

> "An historian dispassionately analysing the evidence to date is almost bound to reach the conclusion that Mr Lawson has gone out of his way to explain how monetary policy is being operated in practice, and how it has evolved, probably more so than any previous Chancellor. [He should be given credit for it.]

Some [ ] per cent of the words on monetary policy have been uttered in this House. The Committee's Report criticises the fact that my monetary speech in April of this year was made outside the House. But I have to say that when I concluded in the ~~the monetary section of this year's~~ Budget, ~~speech with the words~~ "I will say no more about monetary policy", the reaction was scarcely one of deep and widespread disappointment. [Indeed, the Official Report records Hon Members' saying "Hear, hear".]

Today, however, is an opportunity to discuss economic policy, and particularly monetary policy, in detail. The Treasury and Civil Service Committee has produced a serious Report which deserves a serious answer.

The Report suggests that in a number of areas "there has been a substantial change of policy". It starts by allowing that the stated objective of policy has been the same since 1979 - to reduce inflation and to create the conditions for sustainable growth. And it allows that this policy has always had two key strands: firm control of monetary conditions; and reduction of public borrowing. I might say that even this consistency of objectives has not always been a feature of British Governments. But the Report goes straight on to search out changes in the way we have pursued our objectives.

The Report claims that "the operation of monetary policy has become increasingly obscure". Of course, it is an inevitably complicated subject, because it depends on judgements on a number of interrelated variables. But I suspect that the reason that the Committee finds it so hard to follow is that they are making an elementary confusion between the <u>instrument</u> of monetary policy, which is short-term interest rates, and the <u>indicators</u> of monetary conditions, which include the monetary aggregates and the exchange rate.

It is thus completely misconceived to suggest, as the Committee do~~es~~ in paragraphs 8 and 11 of its Report, that we are now giving more emphasis to interest rates and less to £M3. There cannot possibly be a trade-off between the two, because one is an indicator, and one is an instrument.

The Report seems to suggest that I was announcing a change of policy in my Lombard Association speech, when I said that "Short term interest rates are the essential instrument of monetary policy". But this was in fact set out as long ago as 1980, in the Green Paper on Monetary Control, which makes clear that, alongside fiscal policy, the main instrument for controlling monetary growth is interest rates.

Turning to the indicators, the Report suggests that the role of £M3 has become increasingly unclear.

Again, a reading of the 1980 Green Paper ~~makes clear~~ demonstrates that we have never seen £M3 as the sole guide to monetary policy. As we said then, "No single statistical measure of the money supply can be expected fully to encapsulate monetary conditions". In 1980, it did make sense to have only one target aggregate, and one with which the markets were already familiar, because it was important to give a clear and simple indicat~~ors~~ion of our commitment to financial discipline. But in the day-to-day operation of monetary policy, we recognised, to quote the Green Paper again, that "It is insufficient to rely on one measure alone".

We also recognised that the definition used and the choice of target aggregates might need to be adjusted, in the words of the Green Paper, "as circumstances changes" and "in the face of long term changes in the institutional structure". And, of course, that is what has happened. Circumstances have changed, and the institutional structure has altered, with the result that the behaviour of £3M has become increasingly hard to interpret.

It is extraordinary that the Committee's Report makes hardly any mention of these developments. And it is even more extraordinary that there is no reference at all to experience overseas. For UK experience has been similar to that of the other major countries, most of which - including Germany - have found their monetary targets overshooting this year.

We cannot and do not ignore the continued rapid growth of £M3 and other measures of broad money. But for a long period now this growth has proved consistent with continued firm downward pressure on inflation. So it must be tested continuously against the evidence of other indicators. Principal among these is MO - the broad monetary base - which has proved a reliable indicator, with a stable trend in velocity from year to year. This is why, having watched it for some years, we adopted it as a target aggregate in 1984.

The Select Committee say they are not convinced that MO is a useful indicator of monetary conditions. They do not say why, and I suggest they examine the evidence. It is foolish to ~~They~~ imply that all narrow aggregates are misleading because the behaviour of M1 in the early 1970s did not foreshadow the subsequent inflation. ~~But~~ Had they looked at the behaviour of M0 in the early 1970s instead - and I tried to help by pointing them to it in my own evidence - they would have seen that it did, indeed, warn of coming inflation.

[This year M0 has remained within its target range. But its acceleration in recent months was an important factor in the decision to raise interest rates in October by 1 per cent.]

The Select Committee go on to suggest that there has been a volte-face in that we are paying more attention to the exchange rate. Certainly the exchange rate is very important both as a transmission mechanism for monetary policy and an indicator of monetary conditions. In this country, as in the other major economies, it has come to play a more prominent policy role in recent years, as institutional developments have clouded the meaning of the monetary aggregates. But as long ago as 1980 and early 1981, interest rates were reduced because the exchange rate was indicating that conditions were tight, despite a monetary overshoot. The 1982 MTFS explained that (and I quote);-

> "The behaviour of the exchange rate can help in the interpretation of monetary conditions, particularly when the different aggregates are known to be distorted ... the Government considers it appropriate to look at the exchange rate in monitoring domestic monetary conditions and in taking decisions about policy".

The Committee also say - and this is my last point on monetary policy - that policy at present is uncertain. It is said that the Government wants both to prevent interest rates from rising and to prevent the exchange rate from falling.

It is true that the operation of policy is complicated. But - and this is a point I have already made elsewhere and will now make in the House - so is the real world. There are difficult judgements to be made. And the timing of decisions on interest rates is affected by considerations of market tactics. But there should be no uncertainty ~~of~~ about our purpose. As I have said several times, here and in speeches outside, interest rates are and will be set at whatever level, on average, is needed to keep downward pressure on inflation.

Of course no one <u>wants</u> interest rates to be higher than they have to be. But the greatest disservice the Government could do to the economy would be to permit monetary conditions to develop that allowed inflation to take hold again.

The dramatic fall in the price of oil earlier this year meant that some fall in the exchange rate was both necessary and desirable, as the economy adjusted to the lower oil price, without implying a loosening of monetary conditions.

But that was an unusual circumstance. More often, a significant fall in the exchange rate is a clear signal of inflationary pressures, requiring policy action, unless there is reassuring evidence from other reliable indicators such as M0. I will certainly not hesitate to raise interest rates again should that be necessary.

45:1

pvp

FROM: MISS M O'MARA
DATE: 11 DECEMBER 1986

CHIEF SECRETARY

cc PS/Chancellor
Mr Turnbull
Mr Bottrill
Mr Culpin
Mr S J Davies
Mr C W Kelly
Mr D W Owen
Mr S King
Mr Hacche
Mr Pickering
Mr Tyrie
GC/01

AUTUMN STATEMENT DEBATE: 16 DECEMBER

I attach notes on three of the subjects which you thought Mr Gould might raise in Tuesday's debate. Any reference to Mr Gould's behaviour in 1976 (see attached press cutting) will, of course, need care, given current sensitivities about the exchange rate, but I think the sort of tease contained in the balance of payments section (discussed with Mr Culpin) is probably fairly harmless.

MOM

MISS M O'MARA

4529

Manufacturing

Heard plenty this evening about performance of our manufacturing industry. As usual, benches opposite attempting to sell Britain short. To hear them speak, would think that our manufacturing sector had been annihilated.

2. Instead of vague generalisations, let us look at facts.

3. Productivity record under this Government second only to Japan. Risen almost three times as fast as under Labour. Manufacturing profitability last year highest since 1973. And after brief hiccough at beginning of year, experienced by other industrialised countries too, both exports and output rising again, as latest CBI Enquiry confirms.

4. Manufacturing exports up by more than 5 per cent over last two quarters and now stand at record levels. Given hG's attempts to spread gloom and doom, may surprise House to hear that manufacturing industry's volume share of our export markets has held steady since 1980, after years of decline. In fact, no previous 5 year period in our recent history in which manufacturing has so successfully maintained its market share. Strength of exports one of factors sustaining rise in output, up by 10 per cent since last election.

5. Outlook equally promising. Prices of materials and fuel purchased by manufacturing industry 4 per cent lower than year ago and factory gate prices rising more slowly than for last 16 years. On top of this, exchange rate now adjusted fully to oil price fall, sharpening British industry's competitive edge. So forecasting 4 per cent growth in output next year. And figures from DTI Survey published last week suggest 2 per cent growth in manufacturing investment in 1987, with higher growth in 1988.

6. Economic strategy designed to ensure all sectors flourish. Government certainly not neglecting manufacturing. But other sectors important too. Worth remembering that services account for over twice as much of output and nearly three times as much employment as manufacturing. Yet hear surprisingly little from hG about contribution that sector of industry can make.

Balance of payments

HG has made much of our current deficit on visible trade and the £1½ billion balance of payments deficit we are forecasting next year.

2. Must not allow immediate prospect to obscure record under this Government to date. Since 1979, cumulative current account surplus of £21 billion, compared with £5 billion deficit under Labour. And deficit forecast for 1987 only ½ per cent of GDP, compared with the 3-4 per cent deficit which thrust Opposition into arms of IMF in mid-1970s.

3. Emergence of small temporary deficit in 1987 not surprising, given deterioration in our oil balance following oil price collapse, sluggish growth of world trade this year and relatively high level of demand at home. But world trade is now picking up and recent fall in exchange rate, the natural adjustment to halving of oil price, should gradually be reflected in improved balance of visible trade. Signs that UK industry already beginning to respond to increased export and consumer demand. But note hG has carefully failed to acknowledge exports rising in underlying terms - excluding oil and erratics, up by 1½ per cent in three months to October on previous three months - while underlying growth in imports seems to be slowing. And for next year as whole, we forecast non-oil exports will be up by 5½ per cent.

4. But if we are to remain competitive in international markets, vital to conclude lower pay settlements than in past. Hon members opposite would, by contrast, like to accommodate all cost pressures through lower exchange rate. Nothing new. HG himself urged depreciation as route to salvation in 1976. And in those days, Labour Government's standing in market so shaky that policy prescriptions of single backbencher was sufficient to start run on pound.

Squandering North Sea oil

Any talk of "squandering" comes rather oddly from a Party which, when in office, devoted more than 48 per cent of GDP to public spending and borrowed in a single year what would amount to over £35 billion today - although I accept that hG was then too wet behind the ears to sit on the Treasury Bench.

2. But, that apart, his charge simply does not stand up to any kind of scrutiny. It is the revenue from North Sea which has helped this Government to reduce borrowing as proportion of GDP to levels not seen since early 1970s. This restraint on part of public sector has in turn freed resources for private investment. Last week's Investment Intentions Survey suggested growth of 6 per cent in industrial investment next year. And revenues from North Sea have enabled us to reduce level of official overseas debt by around 15 per cent from $22 billion we inherited in May 1979 to around $19 billion now.

3. North Sea has strengthened external account in other ways too. As result of exchange control abolition in 1979, and prudent investment which it permitted, our net overseas assets stood at £80 billion at end 1985, making UK one of world's largest holders. Earnings on these assets, currently totalling nearly £5 billion, will provide us with steady income long after revenue from North Sea runs out.

4. HG, as usual, focussing on wrong issue. Should rather be drawing attention to fact that UK economy has been able to take unprecedented collapse of oil price in its stride. Despite fall in oil revenues of around £6½ billion since 1985-86, PSBR as proportion of GDP (1¾) still half figure achieved in best year under last Labour Government (3½), while growth proceeds at steady pace and number of people in work continues to rise.

Times 27/10/76

etable
n

loan", the sources said. And will make its own views clear the IMF on whether it conlers the conditions attached to e loan to be adequate.

In forming its opinion, the oup of Ten will largely rely an analysis of the British tlook for 1977 that should be mpleted by early December the Organisation for Econnic Cooperation and Developent.

There is no doubt that Mr itteveen will have to seek pplementary currencies from e Group of Ten to finance the n. The IMF's liquidity total usable currencies available to aking loans stood at just 00m special drawing rights bout $6,500m) at the end of gust.

The IMF can obtain up to 00m special drawing rights rough maximum use of the neral arrangements to borw, plus an additional 865m iss francs.

t is questionable whether the nk of England will be able to bilize the exchange rate for pound during the week or that may elapse between time Britain gets its IMF n and the December 9 repaynt date of the $5,300m credit, sources said.

MP's pound rate plea brings fresh setback

By Melvyn Westlake

Sterling, which at one time yesterday appeared to be making a small tentative recovery on the foreign exchanges, suffered another setback after a Labour MP suggested that the exchange rate against the dollar be lowered to $1.50. In the highly nervous state of the currency markets, this comment was enough to provoke a fresh wave of sterling sales. The rate quickly dropped some two United States cents, before closing in Europe at $1.5900, down a net ½ cent.

Up until the late afternoon, trading had been much calmer than on Monday. The pound had been helped by speculation in the *Washington Post* that Britain's minimum lending rate would have to rise to 18 per cent as a condition of the $3,900m loan that is currently being negotiated with the International Monetary Fund. The rate stands at 15 per cent.

The *Washington Post* report was denied by an IMF spokesman who said the fund could not determine its views on detailed measures before its on-the-spot examination of the British economy.

A further rise of 3 percentage points in the MLR would make sterling one of the highest-yielding currencies. Whether it would make sterling a more attractive currency to hold among international bankers would depend on the view they took about the future level of the exchange rate. But the possibility of a further sharp rise in British interest rates prompted the pound to rise to $1.6060 at one stage. The Bank of England was not thought to have given any direct support to the currency.

The late fall in sterling came after a statement by Mr Bryan Gould, Labour, Southampton, Test.

He urged the Government to devalue sterling to $1.50 immediately to restore the competitiveness of British exports. He said that export prices of manufactured goods were no more competitive now than in 1973, and that the pound was by no means undervalued. He told Reuters that he had strong private support for his views among parliamentary colleagues and industrialists.

Mr Gould said that the pound would fall to $1.50 anyway, and that the currency should be devalued to this level, although he did not say how this was to be achieved when exchange rates were floating.

agency reports from T quoted a spokesman for Mi bishi Motors, part of the Mi bishi Heavy Industries Grou saying that a basic agreem had been reached with Chr Europe to assemble a Mitsubishi subcompact ca Britain and on the Contine

Under the agreement, the now being developed would assembled at three Chry plants starting in 1979. spokesman named the parti ants as Chrysler UK, Chry France and Chrysler Spain.

He was reported as say that Mitsubishi would supply to 49 per cent of the comp ents, leaving the remainder be manufactured locally. new car would be sold in E ope as a Chrysler, but was expected to be in direct comp tion with two Mitsubishi models already exported British and continental mark because they were different price, size and design.

Within two hours of th reports reaching London, Don Lander, the head Chrysler Europe issued following statement:

"Any suggestion that th is an agreement to build Mitsubishi car or any oth Japanese car at any of plants in Europe is entirely true. For some time there h been a technical exchange views between Mitsubishi a Chrysler through our joint co pany and for our mutual ben fit and these are continuing

A denial also came from

CONFIDENTIAL

PWP

FROM: A P HUDSON
DATE: 12 DECEMBER 1986

CHANCELLOR

cc: Chief Secretary
Sir P Middleton
Sir T Burns
Mr Cassell
Mr Scholar
Mr Turnbull
Mr Peretz
Mr H P Evans
Mrs Lomax
Mr Sedgwick
Mr Culpin
Miss O'Mara
Mr Allan
Miss C Evans
Mr Tyrie
Mr Ross-Goobey

AUTUMN STATEMENT DEBATE SPEECH: FIRST DRAFT

1. I attach a first draft of the speech, incorporating contributions from Messrs Peretz, Scholar, and Turnbull.

I hope we have picked up most of the points you wanted to make on the TCSC Report. The problem is that the speech is now much too long - there may be as much as 35 minutes' worth here. As well as pruning generally, my feeling is that the section on Big Bang could go, if necessary, and the one on the world economy could be cut down drastically.

APH

A P HUDSON

CHANGES PP 9 & 10

AUTUMN STATEMENT DEBATE SPEECH: FIRST DRAFT

I beg to move ...

I begin by thanking the Treasury and the Civil Service Select Committee, under the chairmanship of my RHF the Member for Worthing, for their report on the Autumn Statement, which, as ever, they have produced with commendable promptness.

In the course of my own evidence to the Committee, my RHF the Member for Worthing suggested that the office of Financial Secretary was older than that of Chancellor. That may depend on definitions. But certainly, recent holders of the post of Financial Secretary have achieved distinction in a number of ways. My RHF is Chairman of the Select Committee. The RHM for Ashton-under-Lyne is Chairman of the Public Accounts Committee, and the RHM for Dudley East was recently voted Parliamentarian of the Year.

I have, of course, been privileged to hold both the offices of Financial Secretary and Chancellor, and only one other person has done this - John Herries, who became Chancellor in 1827. Not a household name, but his career is not without interest. In his maiden speech, he opposed the repeal of the window tax. He resigned as

Chancellor after only a few months - over the appointment of a Chairman of the Finance Committee. And later it was said of him - and I quote -

> "He made the public accounts intelligible, which they never were before."

This is something that I have consistently tried to do, and it is really not fair of the Treasury and Civil Service Committee to suggest otherwise. This Government have been the first to publish the Medium Term Financial Strategy and the first to publish an Autumn Statement. As Chancellor, I have devoted, at a very rough estimate, [ ] words to explaining monetary policy alone. Far from being economical with the truth, I have done my best to explain the truth about the economy. So I was gratified to see this comment in the latest Greenwell Montagu Monetary Bulletin:

Rephrase: [illegible] words! (see eg para [illegible] "the operation of monetary [illegible] has [illegible] obscure"!)

Gordon Pepper talk to Politix Assn on 2 Dec, [illegible] G M [illegible]. Pepper [illegible] Keating [illegible] his advice [illegible].

> "An historian dispassionately analysing the evidence to date is almost bound to reach the conclusion that Mr Lawson has gone out of his way to explain how monetary policy is being operated in practice, and how it has evolved, probably more so than any previous Chancellor. [He should be given credit for it.]

[? how long]

Some [ ] per cent of the words on monetary policy have been uttered in this House. The Committee's Report criticises the fact that my monetary speech in April of this year was made outside the House. But I have to say

AW!

See Kinnock 10/12, col 660

(Rather scant regard for parliament)

that when I concluded in the Budget, "I will say no more about monetary policy", the reaction was scarcely one of deep and widespread disappointment. [Indeed, the Official Report records Hon Members' saying "Hear, hear".]

Today, however, is an opportunity to discuss economic policy, and particularly monetary policy, in detail. The Treasury and Civil Service Committee has produced a serious Report which deserves a serious answer.

Beef up

The Report suggests that in a number of areas "there has been a substantial change of policy". It starts by allowing that the stated objective of policy has been the same since 1979 - to reduce inflation and to create the conditions for sustainable growth. And it allows that this policy has always had two key strands: firm control of monetary conditions; and reduction of public borrowing. I might say that even this consistency of objectives has not always been a feature of British Governments. But the Report goes straight on to search out changes in the way we have pursued our objectives.

Link with Pepper quote

The Report claims that "the operation of monetary policy has become increasingly obscure". Of course, it is an inevitably complicated subject, because it depends on judgements on a number of interrelated variables. But I suspect that the reason that the Committee finds it so hard to follow is that they are making an elementary confusion between the instrument of monetary policy, which is short-term interest rates, and the indicators of monetary conditions, which include the monetary aggregates and the exchange rate.

It is thus completely misconceived to suggest, as the Committee does in paragraphs 8 and 11 of its Report, that we are now giving more emphasis to nominal interest rates and less to £M3. There cannot possibly be a trade-off between the two, because one is an indicator, and one is an instrument.

The Report seems to suggest that I was announcing a change of policy in my Lombard Association speech, when I said that "Short term interest rates are the essential instrument of monetary policy". But this was in fact set out as long ago as March 1980, in the Green Paper on Monetary Control, which makes clear that, alongside fiscal policy, the main instrument for controlling monetary growth is interest rates.

give quote (para 5)

~~an pr.~~ wh..... (check)

Turning to the indicators, the Report suggests that the role of £M3 has become increasingly unclear.

Again, a reading of the 1980 Green Paper demonstrates that we have never seen £M3 as the sole guide to monetary policy. As we said then, "No single statistical measure of the money supply can be expected fully to encapsulate monetary conditions". In 1980, it did make sense to have only one target aggregate, and one with which the markets were already familiar, because it was important to give a clear and simple indication of our commitment to financial discipline. But in the day-to-day operation of monetary policy, we recognised, to quote the Green Paper again, that "It is insufficient to rely on one measure alone".

We also recognised that the definition used and the choice of target aggregates might need to be adjusted, in the words of the Green Paper, "as circumstances changes" and "in the face of long term changes in the institutional structure". And, of course, that is what has happened. Circumstances have changed, and the institutional structure has altered, with the result that the behaviour of £M3 has become increasingly hard to interpret.

It is extraordinary that the Committee's Report makes hardly any mention of these developments. And it is even more extraordinary that there is no reference at all to experience overseas. For UK experience has been similar to that of the other major countries, most of which - including Germany - have found their monetary targets overshooting this year.

We cannot and do not ignore the continued rapid growth of £M3 and other measures of broad money. But for a long period now this growth has proved consistent with continued firm downward pressure on inflation. So it must be tested continuously against the evidence of other indicators. Principal among these is MO - the broad monetary base - which has proved a reliable indicator, with a stable trend in velocity from year to year. This is why, ~~having watched it for some years, we adopted it as a target aggregate in 1984.~~ throughout my time as Chancellor, I have chosen to set targets for narrow money in the form of M0. (Lawson p5)

See also p12 Lawson Speech

The Select Committee say they are not convinced that MO is a useful indicator of monetary conditions. They do not say why, and I suggest they examine the evidence. It is foolish to imply that all narrow aggregates are misleading because the behaviour of M1 in the early 1970s did not foreshadow the subsequent inflation. Had they looked at the behaviour of M0 in the early 1970s instead - and I tried to help by pointing them to it in my own evidence - they would have seen that it did, indeed, warn of coming inflation.

[This year M0 has remained within its target range. But its acceleration in recent months was an important factor in the decision to raise interest rates in October by 1 per cent.]

The Select Committee go on to suggest that there has been a volte-face in policy in that we are paying more attention to the exchange rate. Certainly the exchange rate is very important both as a transmission mechanism for monetary policy and an indicator of monetary conditions. In this country, as in the other major economies, it has come to play a more prominent policy role in recent years, as institutional developments have made the monetary aggregates more difficult to interpret. But as long ago as 1980 and early 1981, interest rates were reduced because the exchange rate was indicating that conditions were tight, despite a monetary overshoot. The 1982 MTFS explained that (and I quote);-

> "The behaviour of the exchange rate can help in the interpretation of monetary conditions, particularly when the different aggregates are known to be distorted ... the Government considers it appropriate to look at the exchange rate in monitoring domestic monetary conditions and in taking decisions about policy".

The Committee also say - and this is my last point on monetary policy - that policy at present is uncertain. It is said that the Government wants both to prevent interest rates from rising and to prevent the exchange rate from falling.

X might go here

Of course no one <u>wants</u> interest rates to be higher than they have to be [or the exchange rate to spiral ever downwards.] But the greatest disservice the Government could do to the economy would be to permit monetary conditions to develop that allowed inflation to take hold again.

It is true that the operation of policy is complicated. But - and this is a point I have already made elsewhere and will now make in the House - so is the real world. There are difficult judgements to be made. And the timing of decisions on interest rates is affected by considerations of market tactics. But there should be no uncertainty about our purpose. As I have said several times, here and in speeches outside, interest rates are and will be set at whatever level, on average, is needed to keep downward pressure on inflation.

The dramatic fall in the price of oil earlier this year meant that some fall in the exchange rate was both necessary and desirable. It was the inevitable response to an unusual event. It did not reflect a loosening of monetary conditions.

But more often, a significant fall in the exchange rate is a clear signal of inflationary pressures. In those circumstances there would be a presumption towards taking action unless there ~~was~~ were reassuring evidence from other reliable indicators such as M0. I will certainly not hesitate to raise interest rates should that be necessary.

?

Fiscal policy

Let me now turn to fiscal policy, where, I have to say, I find the Committee's observations scarcely more coherent. Their complaint here is not that the government's policy has changed, but rather that it is the same. Specifically, they are unhappy that the Autumn Statement reaffirmed the Government's commitment to the same fiscal stance as was set out in the 1986 MTFS.

The reasoning in this part of the Report is, Mr Speaker, frankly obscure. The Committee, spurred on no doubt by their advisers, have decided after all these years to abandon the PSBR as the measure of the fiscal stance. No reasons are given for this change of mind other than the assertion that the PSBR can be measured inclusive or exclusive of asset sales - though this is hardly a surprise since I myself explicitly drew attention to the size of the PSBR excluding privatisation proceeds in the Red Book this year. They then go on to argue that the public sector financial deficit is - I quote - a more "relevant and useful figure". It is a pity that when the Report goes on to give its own estimate of the PSFD for 1987-88 it gives a wholly ~~irrelevant and useless~~ ludicrous figure - of £14.5 billion, which can in no way be reconciled with the £7 billion figure in the same table for the PSBR for that year.

But, important though these details are, they are really just technical errors in this Report. On the main issue, the Committee have, I fear, no advice to offer the House. They question whether the PSBR should be held to ~~1¼~~ 1¾ per cent of GDP next year. But they express no view at all as to what would be the appropriate level at which to set it. On this they are silent.

This deficiency is perhaps understandable. But I find it very hard indeed to understand the justification for the slur which the Committee attempt to cast on the Government's commitment to hold the PSBR next year to $1\frac{3}{4}$ per cent of GDP. The reason given in the Report for this - that any forecast of the PSBR is uncertain and subject to a margin of error - is beside the point, and reveals a rather elementary misconception. When the Chancellor of the Exchequer on Budget day sets the borrowing requirement at a particular figure, he is not making a forecast, and I am astonished that the Committee should misunderstand the Budgetary process in this way. Rather, he is making a judgement about the appropriate fiscal stance, [& sets tax rates accordingly] And this judgement is an essential counterpart to monetary policy in the Government's overall economic strategy.

The PSBR figure published on Budget day is, nevertheless, subsequently validated, or not, as the case may be, by events; and this government's record here is a very good one. The November PSBR figures, published this week, show that public sector borrowing is firmly on course, or below, the level set in the Budget. Last year the PSBR undershot the Budget level by more than £1 billion. And in 1984-85, excluding coal strike effects, the outturn was about the same level as the Budget estimate.

[illegible]

As to the level of the PSBR, it is, at an estimated $1\frac{3}{4}$ per cent of GDP this year, low by any reckoning, below the general levels of recent years, and far, far below the excessive levels from 1974 to 1979, when it averaged nearly 7 per cent of GDP or over £20 billion a year at today's prices. This is the picture whether or not privatisation proceeds are taken into account and it is the picture laid down in successive versions of the MTFS right back to 1980.

Elaborate (extent of [illegible])

[BhC]

Tax cuts

Like other commentators, the Treasury Committee have speculated about what all this means for tax cuts. I decided last year no longer to publish a fiscal adjustment in the Autumn Statement, so as to discourage the pointless and misleading calculations which are always made at this time of year. Subsequent events last winter proved how right I was. But speculation persists.

Let there be no mistake about this. As I have said repeatedly, a pound used in additional expenditure is a pound which is not available for reductions in taxation, unless borrowing increases. But I have ruled out higher borrowing. The increase in public expenditure which I announced for 1987-88, of £4¾ billion, is a very substantial sum.

The House should be in no doubt that the substantial increase in public spending next year has much diminished any scope there might have been for reductions in taxation. Of course the uncertainties are enormous, as

Rephrase emphasis (see over)

[illegible]

we always see in the period between the Autumn Statement and the Budget. But on one point there is no uncertainty, and no shadow of doubt - and that is the Government's resolve to keep borrowing under control, as we have done consistently since 1979; and to take no risks with inflation.

Public Expenditure

On public expenditure, the Committee have again engaged in a textual critique worthy of biblical or Shakespearean scholars to try to demonstrate a major change in direction. Which is odd since much of the material at the back of the report is developing the theme that public spending is returning to a trend.

The true position is very simple. We have long maintained that the state takes too much of the nation's income and its share should be reduced - this can be traced back not only to the 1979 manifesto, but even before that to our policy document "The Right Approach to the Economy". And we have pursued this objective consistently.

It is true that some of the targets we have set ourselves have in the event proved too ambitious. But it is better to attempt to meet demanding targets than to have the complete absence of financial discipline offered by the party opposite.

If it were indeed the case, as the Committee contend, that policy on public spending had been changed this year, one would expect to be able to detect some break in trend.

But the figures show no such break. As I explained at the time of my Autumn Statement, the rate of increase of public spending in real terms, even excluding privatisation proceeds, has been coming down progressively. From 3 per cent in the decade to 1978-79, to $2\frac{1}{4}$ per cent in the last Parliament and to $1\frac{3}{4}$ per cent so far in the present one. Far from reversing that trend, our plans seek to extend it.

Here we are arguing about whether public expenditure will grow by 1 per cent a year, as our plans imply, or $1\frac{1}{2}$ per cent a year as suggested by the Committee. Let me remind the House that the party opposite increased expenditure in real terms by 12 per cent in a single year.

If one looks for a break in trend you will find one certainly, but it was in 1982-83, when the rise in public spending as a proportion of GDP came to an end. In the 4 years since then, the proportion has fallen progressively, and with spending planned to grow significantly more slowly that the economy as a whole, the downward trend will continue, so that by 1989-90, public spending as a proportion of national income will be back to levels last seen in the early 1970s.

[illegible]

I might say, incidentally, that I have been speaking here about General Government Expenditure, because last year, the Committee criticised me for focussing on the planning total and so ignoring debt interest. This year, I have followed their advice, but they now seem to want me to focus on the planning total.

Summing-up of riposte to the Committee

quotes from Lawson's speech (pp 2 & 15/16)

In summary, I have said before that there have been some changes of emphasis in the way different aspects of economic policy have been conducted, and changes of presentation. Indeed, it would be extraordinary if there had not been. Since 1979, there have been enormous changes in world economic conditions, in the position of the UK, and in the operation of the financial markets. The Select Committee, the House, and the country would be rightly concerned if Government policy had not evolved in the light of these developments. But to depict this evolution as "a substantial change of policy" is absurd. If the Committee needs to be reminded of what a real shift of policy is, they need look no further than the last Labour Government. (pre & post IMF)

Of course, if ever there was a year in which I might have been expected to change policy, it has been 1986, with the halving of the oil price. And many people duly advised me to make changes. I rejected this advice, and maintained the same course. And there has been no crisis. Inflation has reached its lowest levels for nearly twenty years. Growth has continued, albeit at a slightly slower rate than in previous years. The number of people in work has continued to rise, and unemployment now looks to be on a downward trend.

The way that both the private sector and the public finances have withstood the fall in the oil price is a remarkable achievement. That is the best possible vindication of the economic policy we have pursued since 1979, a policy which has brought five years of steady growth, low inflation, and a million new jobs since 1983.

For 1987, I predicted a continuation of this pattern, with growth slightly faster than this year, and inflation staying low. The figures that have been released since the Autumn Statement tend to confirm that picture. Output has picked up, with industrial production in the three months to October 1½ per cent higher than in the previous quarter. Exports are up by the same amount, 1984/5 resuming their previous upward trend. The current projection that the surplus on invisibles will be some £750 million contrasts with the view put to the Select Committee by one fellow specialist witness, ~~Mr Bill Martin,~~ who described the earlier projection of £600 million as "particularly optimistic". [Seasonally adjusted unemployment fell by 25000 in October. [Inflation.]]

eh?

— too optimistic?

[This cd be greatly compressed and anti-protectionist message]

The World Economy

The outlook for the British economy will, of course, depend on developments in the world economy.

In the Autumn Statement, I forecast that growth in the major seven industrial countries would average 3 per cent in 1987, slightly faster than this year. The latest industrial production figures released by these countries bear out this assessment. Output in the third quarter in France, the United States and of course, the United Kingdom, was up markedly compared with the second quarter. I expect this upward trend to be maintained into 1987, as the benefits of lower oil prices feed through. Meanwhile, the annual rate of inflation in the seven Summit countries is set to stay low.

Germany? Japan?

And world trade in manufacturing is expected to grow much faster than it did in 1986.

One of the main changes in the world economy over the past 15 months has been the relative fall in the value of the dollar following the Plaza Agreement in September of last year. Plaza itself has been a notable success, both in terms of the cooperation between countries to achieve a given goal, and in terms of the orderly way in which exchange rates have adjusted. So far, we have seen some of the familiar initial effects of currency realignments - the first part of the so-called "J-Curve" effect. In particular, the value of US imports has gone up, and with it the US current account deficit. Similarly, in dollar terms, Japanese exports reached record levels in September of this year. But there are now signs that the tide is turning, which tends to confirm my forecast that Japanese growth might be relatively modest next year. The overall outcome will depend on how far the Japanese implement some of the measures under discussion to boost domestic demand.

Most forecasters expect GNP in the USA and Germany to grow by about 3 per cent next year, though domestic demand should grow much faster in Germany than in the US. This pattern of growth should contribute to reducing the current account imbalance of the two countries.

One threat to the progress of the world economy in 1987 is protectionism, a threat which is greater following the recent elections in the United States. This would be a disastrous step backwards. A major step towards freer trade was taken in Uruguay in September, with the agreement on a new GATT round, to include services and agriculture for the first time. I took the initiative in putting the thorny issue of agricultural subsidies on the agenda for the next round of international meetings. And as far as the United States is concerned, the exchange rate fall which they sought at Plaza, to make their industry more competitive, has now taken place.

My hope is therefore that countries will continue to co-operate to make world trade more, rather than less, free.

The past year or so has seen substantial changes and discontinuities - the halving of the oil price, falls in other commodity prices, and the realignment of exchange rates. And the world economy has adjusted, with merely a pause in the growth of world trade. In part at least, this is because the major countries have cooperated in pursuing soundly based policies. The outlook for 1987 is for faster growth, and it is crucial that we do not lose our way through failures of policy, such as a retreat into protectionism.

Privatisation [not a separate Section — but put paragraph on Gas where privatisation comes in earlier – eg p11]

More and more countries are now pursuing similar policies, not just in terms of broad economic strategy, but of micro economic policies too. A key example is privatisation - a policy which we pioneered, and is now being emulated around the world. This year saw both the French and the Japanese embark on a privatisation programme.

Why no loss?

Our own privatisation programme has taken a major step forward with the sale of British Gas. This has been a triumphant success. Some 5 million people decided to buy shares. Most of them were not seeking to make a quick buck - the offer was widely seen as tightly priced.

Rather, they saw shareholding - and British Gas - as a sound and sensible way to invest their savings. This bodes well for future privatisations, and indeed for the health of industry and the economy in general.

There will be enormous benefits from exposing British Gas to the attitudes and pressures of the private sector, and to the disciplines of the capital markets.

- Customers will gain from improved efficiency, with the regulatory regime guarding against excessive price increases.
- Management will be free to manage.
- And no less than 95 per cent of employees took the chance to buy shares, which sharpens their incentive to succeed.

A further recent illustration of the benefits of privatisation has been the further expansion of Jaguar, where the start of a new night-shift means that 2000 new jobs have been created since privatisation.

Beyond that, there is the benefit of wider share ownership. Even before British Gas, the number of shareholders had doubled since 1979. And the flotation of the Trustee Savings Bank Group and sale of British Gas have revealed the massive widespread interest that now exists in investment in equities.

As on so many issues, the people who are out of step are the Opposition in this House. So I would like to ask the RHM for Sparkbrook a question which is of interest not only to us in the House, but to the 5 million people who have bought shares in British Gas. In the unlikely event of a Labour Government, what would happen to their shares?

I shall gladly give way.

The Big Bang

One other thing for which 1986 will be remembered is the Big Bang.

It is still early days, but the new market structure is working well, with some inevitable teething troubles on the technical side. Market turnover is up by around thirty per cent. Commission costs are markedly lower. If the good progress continues, there will be benefits not just for the City but for the whole economy.

All this could, of course, be put at risk if London lost its reputation as a clean place to do business, and some people have seized on the recent cases of misconduct as evidence that this will indeed happen. However, the fact that these cases have come to light shows that firms are well aware of the importance of maintaining the integrity of the London Market. And the Government's decision to bring the draconian new insider dealing powers in the

Financial Services Act into effect two months early shows that we will take whatever action is necessary to uphold standards.

Taken together, the Financial Services Act, the Building Societies Act, and the Banking Bill, currently before the House, provide a comprehensive framework for the regulation of the whole financial market. And we are also keen to improve cooperation with regulators in other countries to ensure uniformity of standards and exchange of information. Bad regulation must not be allowed to drive out good.

Attack on Labour

1986 has also been a notable year in the annals of the Labour Party. It is the year in which they have reassembled all the economic policies that have failed before, and been rejected by the electorate before. And the year in which they have broken with the traditions of previous Labour Governments by abandoning, in effect, the established defence policy of this nation.

I had better be careful, because if I am too critical of the RHM for Sparkbrook, he may cancel his reply, just as he refused to speak to the CBI last week because they criticised his policies.

The RHM for Sparkbrook may not have had much time for economic policy recently - he has been busy standing in for his RHF the Leader of the Opposition, who has been absent from our affairs playing the world statesman to such disastrous effect for his party. Perhaps this is why, when my RHF the Chief Secretary wrote to the RHG, asking for clarification of his views on Labour's proposed for a training levy on business, he got a very short reply, saying that the HM for Dagenham would be sending an answer in due course. The RHG is clearly too embarrassed to write himself.

But this sort of evasiveness has characterised the RHG's approach to public spending, ever since my RHF the Chief Secretary and I costed Labour's programme at some £28 billion. The RHG has tried to shout down our calculations, and dismiss them as fanciful. Indeed, in spite of this massive programme of spending, and in spite of their record of extravagance when in office and now in local government, the party opposite accused us of going on a spending spree in the Autumn Statement.

We on this side of the House know - and the country knows -that serious economic debate cannot be conducted in this way. The RHG has given no indication of how he would finance his programme, whether by taxation or by borrowing, or both. So I ask him again - out of the massive programme of spending pledges, which would he propose to drop?

??

Conclusion

Mr Speaker, I have, of necessity ranged widely in my speech, because I thought it would help the House in considering the Autumn Statement.

In conclusion, let me come back to the Autumn Statement itself. The Forecast it contains offers the prospect of another year of low inflation and steady growth. It sets out public expenditure plans which make increases in spending in priority areas within a framework in which public expenditure continues to fall as a proportion of national output. It is the latest step in a firm economic strategy which has been pursued consistently since 1979. I commend it to the House.

A

"I am relieved to see the RHG the Member for Sparkbrook in his place today. Because he has ducked a few challenges recently.

- For months, he and his colleagues have refused to answer questions from News International newspapers.

- Last Wednesday, when my RHF the Chief Secretary asked his views about Labour's proposal for a training levy, ~~his answer was that~~ he passed the letter to the HM for Dagenham. ~~would be replying in due course.~~

- Last Thursday, his party spun out the previous day's business so as to spare him the embarrassment of Treasury Oral questions.

- And on Friday, we heard that he had ~~he~~ broken off relations with the CBI, because they criticised his policies.

I have to admit that I, too, have also criticised the RHM's policies in the past. So I am relieved that he has not refused to take part in this debate."