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PART A

Chancellor's (Lawson) Papers:

ENTERPRISE INITIATIVES FOR INDUSTRY AND EMPLOYMENT

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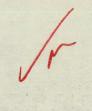
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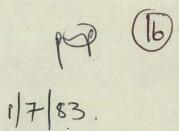
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CHANCELLOR OF THE DUCHY OF LANCASTER







PASSPORT PREUTON S COLKFIELL

PHPER

SECRET AND PERSONAL

PRIME MINISTER

A PASSPORT FOR A JOB

There is, I believe, a large unsatisfied demand for relatively unskilled low paid work while at the same time there is high unemployment. The failure to match the two reflects an unrealistic demand price, the poverty trap and the reluctance of employers - particularly private employers - to get involved in the bureaucracy which goes with employing someone. The problem is particularly acute with the young unemployed. This is an attempt to cut through the knot:

below 18 Age Pay not more than £45 a week No income tax national insurance No employee "protection"

The young worker would be issued with a passport. He would simply lodge it with the employer, who would hold it as his authority to employ the worker without deducting tax or national insurance contributions.

Neither employer or employee would come into contact with the bureaucracy once the passport was issued. There would be no forms, no returns, no anything.

The passport would have a prominent date of expiry printed on it. Once this date was passed there would be an obligation on the employer if he retained the worker to put him back into the system.

There is experience in the use of a passport system of this kind for building workers on the lump.

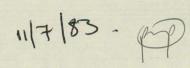
It will, I know, be argued that the employer will hire a succession of young people, firing them immediately they attain 18. This is bound to happen. But the reason it happens is that it is not economic to employ someone on the standard terms applying to those over 18. If we were to reject the scheme on this argument we would be sacrificing a job opportunity for a 16 or 17 year old in an attempt to preserve a non-existent and uneconomic job.

I am sending copies of this minute, on a strictly personal basis, to the Chancellor of the Exchequer and the Secretaries of State for Education and Science, for Employment, for Trade and Industry and for Energy.

1 July 1983







SECRET AND PERSONAL

PRIME MINISTER

A SCHEME TO HELP THOSE STARTING UP AS SELF EMPLOYED

- 1. Our objective is the creation of employment. This will lead to a reduction in unemployment: but it is not the same thing. The creation of employment always adds to the wealth of the nation: a reduction in unemployment does not necessarily do so.
- Both for employment and self employment, tax and national insurance contributions are a serious bar to entry. It is not simply the money: it is the procedures and form filling involved. The obvious remedy of a massive increase in thresholds is completely out of court on grounds of cost: and in the case of national insurance because of the insurance principle. One needs therefore to find some device for getting people at the bottom out without repercussions right up the income scale.
- 3. In order to do this we have to have some means of defining closely the group to benefit: and a definition which is simple; as near as possible automatic; and requiring little or no intervention by the administration.
- 4. I put forward one such proposition in my minute of 1 July. That suggestion referred to the young unemployed. The present suggestion relates to people wishing to set up in business on their own.
- The present VAT limit of £18,000 per annum is sufficiently high to take the new entrant to self employment out of liability in the great majority of cases. We cannot increase it because of EEC regulations but it is not likely to be an inhibiting factor in the present context. But the income tax threshold of £1,785 (£2,795 for the married man) is much too low. So too is the NIC threshold. The Institute of Directors suggested a tax threshold of £5,000. The difficulty of fixing a threshold in profit terms is that one needs to calculate the profit first and this in turn brings the Inland Revenue into the picture. Moreover a simple profit test of this kind too readily invites comparison with the employee.
- 6. What I have in mind is linking the scheme to a training programme either an existing one or one developed for the purpose. I would then link the relief to turnover or takings not to profit.

The outline of such a scheme would be as follows -

A person who had completed the appropriate training course and then set up in business on his own would be exempted from all requirements relating to income tax, VAT and NIC for a period of three years provided his turnover did not exceed £10,000 per annum.

START-- WP FOR SELLP -GINKOYED PREVIOUS COLVERED 7. The £10,000 limit would mean that the man would be outside the VAT et anyway. In most cases the £10,000 turnover limit would mean that net profit would be well under £5,000 pa. And the 3 year limit would ensure that no massive benefit could be secured.

The real sanction however would be the "approved Training Course". This would enable one to eliminate at source the bogus cases such as the "self employed draughtsmen". Moreover the necessity of attending a training course would make the operation unattractive to existing established self employed people.

8. I am sending copies of this minute, on a strictly personal basis, to the Chancellor of the Exchequer and the Secretaries of State for Education and Science, for Employment, for Trade and Industry and for Energy.

COCKFIELD

11 July 1983

REMOVAL OF PRIVATE RENTED PROPERTY FROM LIABILITY TO CGT

General considerations

- 1. Ideal is unsubsidised housing market not easy to acheive (difficult to remove current reliefs for owner-occupiers); but this would go in opposite direction.
- Fiscal considerations do not have significant effect on the size of rented property sector e.g. substantial reliefs in recent years for IIS and CGT.
- 3. Non-fiscal factors e.g. rent regulation and security of tenure likely to be more significant - these are being reviewed by Housing Ministers.

Particular considerations

- Exemption
- Would cost of the order of £m30; (this and the other figures, are very broad estimates only).
- would reduce availability of properties for renting by encouraging sales of existing rented properties for owner-occupation.
- ii. Deferring gain of other assets purchased
- Would cost of the order of £m12/15;
- would provide effective stimulus only if replacement assets had to be tenanted property; but this would reduce its attractiveness to landlords. Encourage sales of rented property and reinvestment in assets yielding larger returns.

Repercussions

- Pressure for relief for other forms of investment which Government may wish to encourage e.g. equities; this would have significant effect on CGT yield;
- pressure from agricultural landlords for similar relief (cost further £m5/6 for exemption and £m3 for rollover relief).

Finance Bill commitment to assist private rented sector

To increase(from £10,000 to £20,000) in FA 1984, with effect from April 1983, the CGT exemption for those who rent part of the property in which they live. DoE Ministers have placed some importance on this relief.

PRIV REVIEW SE TOR

"PASSPORT FOR A JOB" AND HELP FOR THOSE STARTING UP IN SELF-EMPLOYMENT

This note discusses two schemes. The first is designed to ease the problem of youth unemployment; the second, to help those who wish to set up in business on their own.

"Passport for a job"

- 2. This scheme would apply to those under 18, earning no more than £45 a week. A worker falling within this category would be issued with a "passport" which he would lodge with his employer. The employer would hold the document as his authority to employ the worker, without deducting income tax or national insurance contributions and would be exempt from employee protection requirements in his respect. The date of expiry would be printed prominently on the "passport" and if the employer wished to retain the worker's services thereafter, he would be obliged to put him back into the system.
- 3. The essence of the proposal appears to be that under-18s would be willing to accept jobs at lower levels of pay and employers would be more willing to take them on, if they could be relieved of some of the administrative burden and, in relation to national insurance, perhaps some of the cost too. (It is worth noting in passing that employee protection already only applies to workers under the age of 18 in a very limited way. The redundancy and most of the major maternity provisions do not apply to them at all. The unfair dismissal provision requires a qualifying period of one year's employment and it has been proposed that this should be raised to two years it is already two years in small firms.)
 - 4. The arrangements for the scheme as outlined above raise a number of technical difficulties:-
 - (i) if under-18s were exempted from employees' NIC, their employers could be exempted from payment of employers' NIC and NIS. / NIC exemptions would, however, give rise

CONFIDENTIAL

to special difficulty since the contributions buy entitlement to benefits. It would be possible to exclude the employees from this entitlement. But it would not be easy and would provoke requests for similar treatment from others who would be willing to give up benefit entitlement if they were exempt from NIC.

- (ii) If income tax and NIC became payable in full as soon as the £45 limit was passed, a very high marginal rate would be created at that point.
- (iii) It is not clear whether self-employment would be covered.
 - (iv) The scheme might actually make PAYE compliance <u>more</u> complicated for employers if they had to give special treatment to part of their workforce.

However, none of these problems is likely to be insuperable.

- The first is one of equity. It is by no means clear that under-18s should receive specially favourable treatment, particularly through discrimination in the tax system, which is usually expected to be equitable between taxpayers. Indeed, it could be argued that those under 18 are unlikely to have dependents; that because of their low expenses, they get better value out of the single personal allowance than other taxpayers; and that the poverty trap and unemployment trap are less important for them.
- 6. Second, there must be some doubt about the cost-effectiveness of the scheme. Some of the extra jobs for the under-18s would be created by displacing over-18s, although it is impossible to assess what proportion would be affected. Moreover, part of the subsidy would also go to under-18s who would in any event have been in work. In the case of the Young Worker's Scheme which shares a very similar objective, it has been estimated that only about 20 per cent of the jobs receiving subsidy were new ones. (It would, incidentally be for decision whether

- the Young Worker's Scheme should be withdrawn if this proposal were implemented.)
- 7. Finally, there is the risk that an employer will hire a succession of young people who will each lose their job on reaching the age of 18. This is not, however, a conclusive argument. Even a short-lived job would have the big advantage of introducing the young people to habits of work and putting them in contact with the labour market.
- 8. The direct cost of the scheme would be about £60m a year, if only income tax and employers' NIC were involved. If employers' NIC and NIS were brought in also, the cost could be £120m. But these are only the direct taxation effects. To the extent that those receiving the subsidy were in newly created jobs, the PSBR cost would be less because of the benefit savings. But to the extent that they displaced over-18s, the cost would be more. And the upside risk is greater because over-18s pay more tax and receive higher benefits than under-18s.

Help for those starting up in self employment

- 9. Under this scheme, those self-employed who had completed an appropriate training course would be exempted from income tax, VAT and national insurance contributions for a three-year period, provided turnover did not exceed £10,000. (An individual whose turnover is less than £10,000 does, of course, already fall well below the current £18,000 registration threshold for VAT.)
- 10. This proposal poses problems on national insurance and the cut-off point for relief similar to those set out in paragraph 4 above. In addition, it can be argued that any test based on turnover is not appropriate for income tax. The profit of a self-employed person with few expenses, (eg a window cleaner) will be little less than his turnover. By contrast, if a business with substantial inputs (eg a retailer) or considerable expenses on tools or materials (eg a repair shop) has a similar turnover, the owner's income will be very much less.

- 11. These difficulties could be over@ome by redesigning the scheme so that a self-employed person who had completed an appropriate training course would be exempt from income tax on the first £10,000 of his income. This would remove any disincentive to expand beyond the cut-off point.
 - 12. The cost of the proposal would depend on which training courses qualified for the scheme and the extent of the take-up. But based on recent experience of TOPS courses, if around 60,000 adults were to enter MSC courses next year and, say, 7 per cent were to become self-employed soon after, the cost of the scheme could build up to about £8m a year.
 - 13. Although restricting the scheme to those self-employed who had completed some form of training would limit the Exchequer cost, it would also necessarily imply discrimination between one new business and another. It would be argued that relief from tax should not depend on whether those entering self employment needed, or had the benefit of, a training scheme and however the qualifying schemes were defined, there would be those who would fall on the wrong side of the line and would complain they had been arbitrarily excluded. Indeed, it might be suggested that those who had enjoyed the benefit of a training scheme (and had probably paid no fees, if the scheme were provided by the MSC) were the last people to deserve further thelp through a selective tax relief.
 - 14. Second, there is a case for saying that a much clearer dividing line should be drawn between the areas of employment and self-employment before exposing it to further pressure by increasing the relative attraction of Schedule D (Self-employment). Indeed, the scheme would give an added incentive to represent employment as self-employment through such devices as labour only sub-contracting arrangements.

15. Finally, there must be some doubt as to whether the scheme would achieve its purpose. The most critical period in the survival of a small business typically comes after about 18 months. At that time, a business will often not even have been assessed to tax for its first year. And, even if it has been assessed in its first year's results, the tax bill will often be fairly small. The extra expenses of setting up a business and getting it off the ground, the likelihood of capital expenditure which will attract tax allowances, and the fact that turnover is generally only starting to build up in the first year, mean that a new business' taxable profits may often be quite Moreover, because of the way the profits of small or non-existent. a new business are assessed to tax (the first year's results form the basis of tax assessments for, in general, about 22 years liabilities), the existing rules already have the effect of minimising liabilities in the early years.

Enterprise allowance

16. Given these objections, a different proposal to encourage the unemployed to set up in business could be considered. An enterprise allowance has been introduced nation-wide this year, under which a grant of £40 a week is paid for a year to unemployed people going into business. (subject to a maximum of 25,000 places). The future of the allowance is to be decided as part of this year's public expenditure review. If the allowance is continued, then there could be a case for making it non-taxable in order to increase the benefit to the successful. This would, however, point up the taxability of unemployment benefit.

HM Treasury 19 August 1983



DEPARTMENT OF TRADE AND INDUSTRY 1-19 VICTORIA STREET LONDON SWIH OET

Telephone (Direct dialling) 01-215) 3781

GTN 215) " (Switchboard) 215 7877

From the Parliamentary Under Secretary of State for Industry

John Moore Esq MP Financial Secretary to the Treasury Treasury Chambers Parliament Street London SW1P 3AG

Mr Fourmer-IR Monari Gordon Pirie randren

Willetts

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2nd April

ear John

I have already written to Nigel Lawson to tell him how much I welcome the strong enterprise theme in the Budget. I am convinced that this will be a great help in strengthening and encouraging the growth of the small business sector.

Given that the Budget shows such commitment to small business I was a little disappointed by your letter to me of 22 February. I had intended to show a copy of your comments to several small firms lobbyists to demonstrate that we are discussing seriously the complaints which they frequently make to me about PAYE procedures. However the reference in your letter to small employers payrolling work as a "spare time" activity - rather than an integral part of running a business - struck an unfortunate note which would certainly not be well received by the small firms organisations. I trust that this was just a slip on someone's part and does not reflect an outdated attitude to small business which I had hoped would have been long banished from Whitehall.

I realise that the precise level of cash flow benefit to employers operating PAYE is open to debate, however as you acknowledge in your letter the compliance costs for most small firms will be in excess of any cash flow benefit they receive. This of course is why the complaints I receive on this subject make no mention of a cash flow benefit. My officials will certainly investigate further the use which small firms might make of computerised payrolling services, but clearly this course of action will not appeal to the smallest employer and is therefore unlikely to alleviate the alleged serious deterrent effect of PAYE compliance procedures on the potential first-time employer.

I should be grateful for your suggestions on how the administrative burden on small firms of PAYE/NIC compliance procedures might be reduced. A complaint which I often hear is that the presentation of the PAYE 'starter' package of leaflets given to a new employer could be improved. In particular there would seem to be a need for a more clearly marked 'key' to the package explaining how to



operate the system. I would be interested to hear any other ideas you may have on simplifying procedures for small firms. Perhaps we could discuss the subject again soon.

Jours end

DAVID TRIPPIER



From:

INLAND REVENUE POLICY DIVISION SOMERSET HOUSE

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REVENUE DA

18 April 1984

MR BLYTHE 1814

PS/FINANCIAL SECRETARY 2.

PAYE COMPLIANCE COST: MR DAVID TRIPPIER MP

- In his letter of 2 April, Mr Trippier suggests a further discussion with the Financial Secretary. We have assumed that the Financial Secretary would prefer, at least in the first instance, to reply to Mr Trippier's letter. A draft reply is, therefore, attached.
- We were not aware of Mr Trippier's intention to show a copy of the Financial Secretary's letter of 22 February to small firms lobbyists. Mr Trippier refers to complaints he receives but unfortunately does not specify the nature of these complaints. (In recent months, I am only aware of one such complaint being transferred for reply by Treasury Ministers from Small Firms The draft reply, therefore, offers to supply a letter which would be suitable to be shown to lobbyists provided more specific information is given about the nature of the complaints made.
- is attached. Mr Trippier's officials have seen and commented on the text before it reached its final form. This leaflet is

PS/Economic Secretary C. PS/Minister of State Mr Monger

Mr Lovell Mr Gordon

op copy

only)

Mr Pirie

Mr Andren Mr Willetts Mr Isaac

Mr Blythe

Mr Allen (M4/3)

Mr Farmer

Mr Foers

Mr Hann

Mr Fraser PS/IR

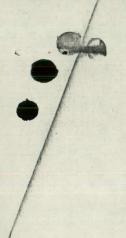
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A copy of the printer's proof copy of our new leaflet (IR53)

DUE

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intended to give a potential employer an insight into what will be involved in operating PAYE/NIC. We do have under review the content and format of the forms and instruction books we send to new employers and have made some progress. However, the staff resources available are very limited and we have, on the whole, to give greater priority to forms and booklets which have a wider application; in particular, those that are sent to and used by taxpayers.

J. Francis

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PS/Minter of State
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Provided
P

Treasury Chambers, Parliament Street, SW1P 3AG

Mr Fraser IR PS/ Inland Neverul

David Trippier Esq MP
Parliamentary Under Secretary of
State
Department of Trade and Industry
1-19 Victoria Street
LONDON

27 April 1984

Dan David,

hank you for your letter of 2 April. I am glad to note that you think the Budget will prove to be of considerable help in promoting the growth of the small business sector. I agree, of course, that it is right that we should look carefully (but realistically) at any activity of Government that may be represented to us as a hindrance to this growth. With this in mind, let me set out in a bit more detail how we have approached the question of compliance costs and PAYE.

In his article on the compliance costs to employers of operating PAYE/NIC, Professor Sandford reported that, of the total gross compliance cost for all employers (£449m), about one-third represented the value of time spent on this task by "directors, partners or proprietors". This indicates the extent to which proprietors do this work themselves. I can understand the feelings of hardworking small businessmen who find they have to set aside some of their very precious time to do payrolling work. It was against this background that I used the phrase "in their spare time". My point simply is that the use of the proprietor's time in this way, although not involving an obvious outlay of cash, may in some instances by costing the business more than the use of a payrolling service, particularly if the proprietor would otherwise be spending that time doing something more productive from the point of view of the business.

I note what you say about the measure of the cashflow benefit. Nevertheless, I do think it perfectly reasonable to draw to the attention of those who complain about their gross compliance costs that this cashflow benefit does exist and should be regarded as an offset against that cost — as also should the fact that the actual costs incurred are allowed as an expense in computing the firm's own tax liability.

You asked about ways of reducing the burden of operating PAYE. We have already taken a number of steps to simplify the operation of PAYE: the structure of PAYE coding has become steadily less complicated in recent years, and we have continued this process with the adoption of the scheme for mortgage interest relief at source last year. This means that the employer has fewer code changes to operate. When we took office in 1979 the small businessman had to cope with PAYE Tax Tables some 500 pages long, but when we removed the lower rate band of tax in 1980 we were able to reduce them to about 50 pages. The right course, I am sure, is for us to continue to seek ways of this sort to make tax collection simpler, both for businesses and for the Revenue.

You referred to the "alleged serious deterrent effect" of PAYE procedures on the potential first-time employer. The Inland Revenue have, in fact, prepared a new leaflet (IR53) "Thinking of taking someone on" which is designed specifically to seek to allay the fears of potential employers. This will be published next month and I understand that your officials have agreed that copies should be available in your Small Firms Centres. Other forms and booklets are kept under review: in particular it is hoped that a revised instruction booklet on the operation of PAYE/NIC and a revised key to the "starter" package can be brought into use in time for the beginning of the next tax year.

i did not realise that you were hoping to be able to copy my letter of 22 February to several small firms lobbyists. If you can let me know the nature of the complaints most frequently made to you, I would be happy to let you have my comments in a form suitable for passing on. I must emphasise, however, that I do not consider that it would be appropriate to provide special relief for small employers from any of the obligations placed on employers as a whole.

JOHN MOORE

POLICY UNIT NOTE ON JOBS

The Policy Unit has now completed its work on the subject of jobs. We have visited Merseyside, Consett, Corby, the Scottish Development Agency area, London Docklands and the Highlands and Islands Development Area. We attach some comments based on our regional visits.

The long-term solution to unemployment is the creation of an economy where markets function properly. Companies have to respond to demand, have to find it profitable to invest, need to draw on skilled people for design, marketing, production and management; and people need a relatively free labour market so that they can move around with ease.

Much of the work under way within Government will help in this task. The Youth Training Scheme and technical and vocational initiative should help in training people into jobs. The MSC initiative to make training more relevant should be pursued vigorously. The Budget has begun the process of removing bias in the tax system against employment and in favour of capital investment. The changes already undertaken in trade union law, and the modifications to the Employment Protection Act, are helping to create a freer labour market. But much more remains to be done. competition policy initiative can also assist in encouraging new business and creating new opportunities.

Policies towards small companies, international trade and the lowering of administrative burdens also need carrying further, and are a vital part of any programme to make markets work. For example, there are too many local authority licensing regulations; tax is still too bureaucratic and complex for small employers; Wages Councils are troublesome; employers still worry about the Employment Protection Act; and the small business measures need rationalising. Similarly,, the housing market needs improvement so that more rented accommodation is available in areas of better job prospects.

Our general conclusions were:

- It is usually better to subsidise people rather than 1. companies.
- The attitude of the local authority to the 2. regeneration of the region is all-important. Where a sympathetic local authority was prepared to work with any other bodies, and assistance that came from Government action - as in Corby - results could be most impressive. Where local authorities were less keen on the endeavour - as in London and on Merseyside success could only be achieved by setting up an independent corporation able to cut through the red tape.

LARABK

POLICY UNIT HUIE OH A DE CONTRACTOR OF BUILD

- 3. Scattering subsidy and assistance over a very wide area without clear targets achieves little. Regional assistance for the whole of Merseyside has not been encouraging and, indeed, part of the problem was the inducement offered to firms like BL and Ford to set up plants in relatively hostile conditions which could not stand the test of time.
- 4. We found that monitoring of the effectiveness of measures in creating jobs which might be self-sustaining could be tightened up. It is important that jobs are not just subsidy-dependent, so we need to know how companies and individuals fare in the longer run. We need a better idea of relative costs and successes.
- When presenting the Government's policies, it should be made clear that there is no inconsistency of purpose between the general drive to create jobs by making markets work, and the measures being taken to alleviate particular distress or to help individuals get back into the employed world. Ministers could help publicise successes in places like Silicon Glen and Corby, where temporary subsidies have helped create jobs that will be self-sustaining in the long run against the original odds of the region. They could help publicise schemes in places like Sheffield, Bristol and London, where the Community Programme and the VPP are giving individuals welcome temporary occupations and making a useful social contribution at the same time; and could draw attention to the excellent work of the Docklands UDC in London in completely transforming a whole area which had been left as a wasteland through the planning controls of hostile local authorities.

Finally, we looked at the careers and histories of some successful entrepreneurs and their companies. There were few common threads, with the exception that specialisation in certain kinds of electronics, and certainly in electronic component distribution, was a good way to develop a fast-growing company which was likely to be successful. The entrepreneurs we looked at all had the stamina and the courage to overcome press hostility and scepticism, to concentrate on making money as their prime aim, and to take calculated risks. Some of the immigrant communities produce more than their fair share, probably because other avenues for social advancement were less easy. Few of them had been to business school: it seems difficult to train entrepreneurs. However, it does seem possible to incrase

LARABK

the rewards for success and to make entrepreneurship an option that is discussed in schools, training colleges and in the community at large, so that more people decide to give it a go.

We con was how would be a way

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APPENDIX

VISITS TO SIX AREAS

We chose six areas where particular employment difficulties exist and where Government has created special agencies and allocated special funds to alleviate the worst problems. Our visits were of one or two days' duration only and do not represent detailed economic or social studies. Our aim was principally to gain an impression of each and to contrast what was being done.

The six areas are - London Docklands;

Merseyside;

Corby;

Consett; and parts of the areas

covered by the Scottish Development

Agency and the Highlands and Islands

Development Board.

The main conclusions we came to are these:

- 1. Not all areas are equally suitable for 'rescue'. Two London Docklands and Corby have decisive advantages of location
 which will enable them to share in the benefits of general economic
 recovery and to shed their 'special area' status in time. In
 our judgement, the other four areas will remain a special charge
 upon the Exchequer for as far ahead as we can see. We should
 not be deluded into thinking that an even heavier allocation of
 public funds will enable these areas to conquer much larger economic
 forces which cause greater activity elsewhere.
- 2. Liverpool is a unique case. It has some disadvantage of location trade flows now being more intense in the south and east of Great Britain compounded by the failure of artificial 'reindustrialisation' of the 1960s and 70s, and capped by the lunatic policies of Liverpool City Council. Industrial regeneration cannot be simply or quickly bought for Liverpool. Some degree of depopulation is inevitable and right. Assistance should help

adjustment towards the smaller economic entity, not try to revive the grandeur of earlier decades.

COMMITTER

- 3. The various development agencies created to attract industry into problem areas have all been 'successful' on a limited scale. The important qualification is that, without exception, they have merely helped to influence the location of economic activity, not added to it.
- 4. With the exception of the Highlands and Islands Development Board, which does not have major conurbations to contend with, all the other areas require attention to land assembly and disposal. Without a supply of land which has either been part developed or is freely available for development, nothing will happen to generate economic activity.
- 5. Since land assembly is vital, so too is the relationship between development agency, planning authority, (usually the local authority) and the landowner (often the local authority). In some cases London Docklands and Liverpool Docklands the development agency was freed from any obligation towards the local authority and was given unfettered power to develop and dispose. In others Corby and the Scottish Development Agency a satisfactory working relationship between development agency and local authority has been consciously erected. In Liverpool (outside the area of the docks) there is ruinous confrontation.
- There is no one right model which makes others wrong. But we observe most 'success' where the development agency is granted sweeping powers and focusses its effects on small areas; or where the local authority adds its weight to the other agencies.
- 6. In general, the evaluation and monitoring procedures adopted for special assistance are poor. Hundreds of millions of pounds are being spent without clear objectives. There is an urgent need to establish, at very least, a robust mechanism for identifying what our expenditure has bought.

COMPLETE

AREA REPORT 1

LONDON DOCKLANDS

Special Expenditure

The Docklands Development Corporation is responsible for the rehabilitation of 5,000 devastated acres where only 37,000 people lived in 1981.

In the first two years of its life, the DC spent £75 million. The bulk of this cash was spent on acquiring and preparing housing land (£22m) and industrial and commercial land (£23m). The Enterprise Zone road, Surrey Docks distributor road and Beckton roads cost £6m. Budgets for 1983-86 show planned spending of £202m including £27m on the Docklands light railway, £58m on land, £22m on environmental improvements and £26m on roads and transport.

The land assembly and preparation is essential. Once developed the land is sold on to new owners and the money returned, often with the benefit of some planning gain. The infrastructure expenditure enhances the receipts on the land transactions and is central to creating the desire to buy docklands properties. The UDC retains influence over the style and purpose of the buildings by refusing to sell freeholds to any developer: the developer holds land under a licence which gives the UDC powers to influence the development. In the main the use of this power has been benign.

The Value of the Expenditure

The results of the expenditure, the enthusiasm of the UDC staff and the powers given to the UDC to acquire land are impressive. At Hays Wharf, after 15 years' delay under the old planning authorities, 40% of the area is going ahead for comprehensive office redevelopment. At nearby Cherry Pier and Cherry Gardens, an 8-acre site is being prepared for housing development by the private sector. In the Surrey Docks, where the DC owns all the land, they are busy stabilising and putting in basic services prior to bringing in the private sector.

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North of the river, around the Limehouse Basin and the West India Dock, a 1,25 million square feet of industrial development is under way. Thirty per cent is already pre-let or owner-occupied, with a concentration on higher technology industries. The UDC has specialised in putting in high-quality red brick roads which are themselves an attractive feature, and a comprehensive ducting system to take fibre optic cables to ensure high quality telecommunications. It has a great advantage as a development operation in that it is not governed by the traditional planning regulation distinctions between industrial and office accommodation, and therefore its high technology buildings have been easier to design and build. The super-stores are also attracting considerable clientele, and are a great boost to the area.

The results are photogenic and show just how dramatic the change in a derelict area can be when the pump is primed by enthusiasts armed with reasonable planning and acquisition powers. Houses have been sold in Beckton in the £28,700 to £34,000 price range and former council tenants have been keen buyers. 3,500 houses have been built or started since 1981 and 3,500 jobs created. The UDC is not a plan-making body and this can cause delays. The concept is difficult to apply to more thickly populated areas where the override of local councils would be difficult to defend. Success in rehabilitation can lead to rapid escalation of land prices which then limits the opportunities for providing low priced housing for council tenants from adjacent estates. In the case of the London UDC they need rapid decisions on the light railway and the VSTOL airport to sustain the momentum.

Most recent figures suggest that for every £1 of public capital invested some £5 of private capital is forthcoming. The ratio should improve over time, and as the full 5,000 acres near completion of development the UDC should receive back much of its cash from land sales. The initial budget costs should be quite large in order to assemble sufficient land and put in the correct infrastructure to have some impact on the problem.

Collins

It is difficult to see what Enterprise Zone status would add to the advantages of the UDC. If there was to be an EZ in London it is important it does not act as a counter-magnet to the UDC.

AREA REPORT 2

MERSEYSIDE

Special Expenditure

Merseyside is classed as a Special Development Area and as such it attracts the highest available rates of Regional Aid. The Regional Development Grants which the Merseyside SDA receives are (at roughly £100m p.a.) far higher than for any other SDA in Great Britain. The amount of Regional Selective Assistance spent in Merseyside is of the order of £10m p.a.

In addition, Merseyside is provided with its own Task Force, which has a current year budget of £40m; and with a Merseyside Development Corporation, which is Government funded at present to about £30m p.a.

There are no exceptional expenditures undertaken by the Manpower Services Commission for Merseyside or for Liverpool.

In total, the expenditure advantages which the Merseyside SDA enjoys over a non-assisted area is of the order of £200m p.a. - equivalent to roughly £350 p.a. for each household in the SDA.

Population and Industrial Employment

Merseyside's population is in long term decline. The Met County population fell by 8.5% (to 1.5 million) in the 10 years 1971 to 1981, while that of Liverpool fell even further - by 16%, from 600,000 to 500,000 over the same period. Nevertheless, economic decline has proceeded faster than shrinkage of the population, with the result that unemployment has risen in the SDA from 12% to 20% over the period February 1980 to February 1984. In recent years, nett job losses have run at between 10,000 and 15,000 per annum.

The traditional large employers in and around Liverpool - the port, shipbuilding and repair, shipping services, and the processing and distribution of edible oil products - no longer enjoy the geographical and competitive advantages of past decades. It is

extremely unlikely that they will return to former levels of employment. Even the larger Merseyside based employers who are not consciously emigrating - Littlewoods, Unilever, Bibby, Ford, for example, are shedding labour to stay competitive.

MSC (locally) and the Task Force take the view that general economic revival in the UK will largely pass Merseyside by. Why should industry want to come to Merseyside? There are few sectoral roots there. Industrial relations, as a generality, are difficult - there is just too much weight of anecdotal evident for this to be denied. Wage rates do not reflect local unemployment levels (MSC maintain, for instance, that building trades rates are the highest in the UK outside London). There is no pattern of new job creation, and (again according to MSC) Merseyside is well below the national average in its proportion of self-employed.

The policies of Liverpool City Council present a serious obstacle to hopes of recovery. The ruling Labour Group, which has been in control of the Council since last May, makes no secret of the hostility to private enterprise, and its disdain for the principles of prudent financial management. Instead it has refused to increase rates or to make savings, while creating a privileged clientele among council tenants and employees.

At present the Council is pursuing a deliberate strategy of seeking confrontation with Central Government. Whether this happens depends on the acceptability or otherwise of its budget for 1984-85. Whatever the outcome the implications for job prospects are alarming, with massive rate increases and further damage to the economic infrastructure and the reputation of Liverpool.

Any future initiatives to help solve the problems of Liverpool will have to take into account the difficulties raised by its local politics, and where possible by-pass them.

The Value of Special Expenditure

What is our £200m p.a. of special expenditure intended to buy? The answer is that we do not know, since neither Regional Assistance nor the Urban Programme have quantified objectives, whether in job terms or otherwise.

CONT

The task is essentially that of humanely managing the contraction, and an important part of that task is to prevent the insidious growth of physical dereliction. It costs relatively little to replace shattered buildings and streets with basic greenery. It does absorb a little labour, and it does not engender false expectations of new jobs.

With this in mind, we strongly support measures such as the restoration of 'key sites' in and around the City Centre. The sites include those round the Anglican Cathedral, the old Exchange Station, and the disused Tate and Lyle sugar refinery. But above all we applaud the creation and the efforts of the Merseyside Development Corporation, whose task is to clear and restore, for private sector development, 865 acres of derelict dockland, nearly all of it on the Liverpool bank of the Mersey.

The key issue is undoubtedly land - its acquisition, management and development to a point where the private sector shows rooted interest.

The Development Corporation and the Task Force

What particularly appeals to us about the Merseyside Development Corporation is:

- its remit (and determination) to do a high quality job on a limited areas of land
- its business-like organisation and style of project management
- its right to act independent of the Local Authority
- its involvement with the private sector currently via local consultancies and contractors and eventually via housing and commercial developers.

COMME

MDC seems to us to represent a good, though not the only, model for tackling urban dereliction. A Development Corporation, it must be said, is not a cheap option, at least initially. But it holds a very good prospect of the repayment of public sector investment.

We question the continuing role of the Task Force, though not the dedication of its members. It has inherited a finite number of projects from the Michael Heseltine initiatives but lacks the power which the MDC enjoys to get things done. The Task Force is constrained to act through Local Authorities, and finds itself obliged to pour lubricant into the points of friction between the City Council, the Met County Council, the DTI, the MSC and the DoE's own programme.

We urge Ministers to consider replacing the MTF, once existing commitments are fulfilled, with one or at most two new bodies similar to the MDC to tackle other <u>limited</u> areas of severe dereliction. Deregulated bodies working on a limited canvas will achieve far more, far more quickly, than bureaucracy working across a large tract.

CONTITUTE

AREA REPORT 3

CORBY

Special Expenditure

Corby was designated a Development Area (the middle of the three tiers of Assisted Area) in late 1979, and in 1981 was authorised to declare 280 acres of development land as an Enterprise Zone.

It has no separate Development Corporation, nor is it a significant recipient of Urban Programme expenditure or of special expenditure by MSC. But the town does have the Corby Industrial Development Centre (CIDC), run by an energetic Ulsterman, Fred McClenaghan, whose task is to market the benefits of Corby as a location for industry. CIDC runs no substantive programme of its own, but has an advertising and administrative budget of less than £500,000. CIDC is funded as to 70% from the New Towns Commission and the balance from Corby District Council, which is moderate Labour-controlled. CIDC reports jointly to its two sponsors, and operates effectively at arm's length from both.

DTI has spent, committed or offered £37 million to Corby since 1979 - £14 million via Regional Development Grant and just over £23m in Selective Assistance. Since that date, 4,000 jobs have been created, 2,000 more are known to be in process, and 3,000 more are expected if companies' plans materialise. If we count only the 6,000 or so jobs which have been or will be created, the cost per job is a little over £6,000 - a long way below the £35,000 national average quoted in Norman Tebbit's recent White Paper.

To look at it another way, each of Corby's 20,000 households has had a contribution of about £379 p.a. over the last five years - more or less the same as the Merseyside SDA.

Population and Industrial Employment

The Corby population is of the order of 50,000 and the available workforce around 27/28,000. Until 1978, British Steel (formerly

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COMMITTER

Stewarts and Lloyds) employed over 11,000 on steel making and tube forming. Steel making has closed, and the site has been cleared. Tube forming continues, but rationalisation with parts of TI will happen eventually. BSC employees are now down to 3,000 and further losses are inevitable.

The efforts of CIDC have come nowhere near mopping up the labour shed by BSC, but there can be little doubt that their efforts have contained what would otherwise have been a very painful result. CIDC estimate that, with the BSC closures and downstream effects, Corby's unemployment rate would have reached 35%. In fact, unemployment peaked at 23% in mid-1981, had fallen to 19% by July 1983, and is still in the 18/19% area.

Corby's attraction to industry is a combination of its location and the Development Area/Enterprise Zone advantages. It lies within 20 miles of the M1, M6, M45 and A1 and is thus an excellent point for businesses which are largely or wholly dependent on distribution. If and when the A1/M1 link is completed, its locational advantage will be substantially enhanced.

Prominent names have been attracted. In alphabetical order, they include Avon Cosmetics, Aquascutum, BAT, BXL, Commodore Business Machines, Electro-Components, Oxford University Press, Rank Hovis McDougall, Tesco and Weetabix. The two largest projects in job terms are CBM (1,100 jobs) and Electro-Components subsidiary, RS Components Ltd (600 jobs). Althoughthere are large numbers of very small businesses springing up, Corby has succeeded (where Merseyside has failed) in bringing in sound medium-sized businesses in the 100 plus employee category.

The Enterprise Zone has been spectacularly successful in attracting new investment. The Corby EZ, at 280 acres, is about 5% of total EZ acreage in the UK, yet has pulled in 39% of total investment. The private producer investment, at just under £43m, is very nearly as much as all other private producer investment in EZs in the UK. The attached summary tells a fuller tale.

Total investment in site development by type of investor, 1 June 1981 - 31 May 1983 (1), £000

	Public developers	Other public author-ities	Private producers	Private, developers, financ. instits.	Other private	Total
Salford	-	-	2,268	4,867	735	7,870
Trafford	rategor - sector	-	37	3,071		3,108
Swansea	2,024	1 - 1 - 1 - 1 - 1 - 1 - 1 - 1 - 1 - 1 -	8,423	2,189		12,636
Wakefield -	290	-	179	640		1,109
Clydebank	10,243		4,998	1,250	-	16,491
Dudley	-	120	3,813	3,956	125	8,014
Hartlepool	1,918		393	581	-	2,892
Corby	17,630		42,673	1,265	- 1991	61,568
Newcastle	212	-	7,841	650	-	8,703
Team Valley	3,557	29	890	2,785	- 1	7,261
Gateshead	230	99 .	1,364	-	_	1,693
Speke	1,577	-	349	650	-,	2,276
sle of Dogs	100	1,780	9,598	4,425		15,903
Belfast (2)	32	-	1,675	420	312	2,439
Belfast (3)	-	-	3,072	1,821	459	5,352
Total	37,813	2,028	87,573	28,270	1,631	157,315
	8 24	1	56	18	1	100

⁽¹⁾ For the Isle of Dogs and Belfast, the monitoring period started in September 1981 and October 1981 respectively.

Source: YEALDS

(This is page 21 from 'Monitoring Enterprise Zones' by Roger Tym and Partners, published in January 1984)

⁽²⁾ Inner City section (3) North Foreshore section
Note: These figures cover all developments under construction at 31 May
1981 or begun since.

y EZ is now fully committed, and the town is

The original Corby EZ is now fully committed, and the town is pressing for EZ designation of a further 25 acres, contiguous with the existing area and sited on land cleared after the closure of the steelmaking plant. Prima facie, it is difficult to see why Corby's request should not be granted.

Potential Problems

The success of CIDC, which they themselves would describe as only a little more than moderate, depends crucially on good personal relationships between the District Council, the County Council and CIDC itself. Institutionally, the arrangement is not durable. A change in the attitudes of the District Council or at the top of CIDC could have difficult repercussions for industrial development or land regeneration. There is no one right recipe which makes all others wrong, but pragmatic cooperation between interested parties is of course indispensible to any solution.

AREA REPORT 4

CONSETT

Population and Employment

Consett lies in Derwentside District Council, a community of some 90,000 people, 14 miles south west of Newcastle upon Tyne. Consett's traditional industrial dependence was on coal and steel. Coal had been in serious long-term decline by the time steel closures began to bite. Peak employment in local pits reached 17,000 but the last pits closed in 1980. Serious run-down at BSC got under way in 1978. In the two years to September 1980, 1,000 jobs had been lost, then BSC closed the remaining facilities entirely, with a further loss of 3,500 jobs. In the ensuing two years, there was major contraction in other local manufacturing industries, most notably at RHP Limited (bearing manufacturers) where a further 1,250 jobs were shed in 1981.

At the time of the final steelworks closure, BSC accounted for over 12% of total local employment. The unemployment rate in north-west Durham was then already nearly double the average for Great Britain (15.5% against 8.3%) and the effect of the BSC closure was to send the local rate to just over 25%.

Special Expenditure

Consett was already a Special Development Area by the time of the final steel closure and therefore qualified for the highest level of regional aid. The area also attracts European Coal and Steel Community aid, especially low cost loans, and will be a special programme area under the European Regional Development Fund non-quota section.

As a steel-closure area, Consett received initial support from BSC Industry. A grant of £10 million was made for clearing and landscaping the steelworks site, and provided funds for advance factory building, special manpower measures and support for loss of rate income. The English Industrial Estates Corporation put

in £12.6 million over five years for a potential 650,000 square feet of advance factories capable of accommodating some 2,500 jobs. Over the three years to December 1983, £2.6 million was paid in selective financial assistance to 24 projects which accounted for 1,000 new jobs and safeguarded 160 more.

The Derwentside Industrial Development Agency was set up in 1982 on the initiative of BSC, with six staff. Its first objective was to maintain the momentum of industrial regeneration begun by the District Council and BSC Industry. Initial donations of £120,000 were provided by BSC Industry, the District Council and local firms. DIDA, in its first year, attracted 800 new jobs and plans to attract a further 1,000 this year. DIDA runs on a budget about one-fifth that of Corby for a population about 50% greater. Furthermore, Consett has no Enterprise Zone.

DIDA, in the commitment of its staff and in the results it achieves with few resources, is one of the more impressive agencies we visited. Its particular strength is in the evaluation and monitoring of projects whose sponsors have applied for aid.

The proponents of each potentially aid-worthy project are helped to produce a detailed business plan setting out forecasts of sales, jobs, product descriptions, markets and costs and including the curricula vitae of the directors. DIDA plans suggest that there will be about 3,500 new jobs over the next three years.

The Agency carries out an annual job audit, monitoring 180 companies and projects, each year, at about the end of March, every company is telephoned to check the number of people employed, performance against the plan and any necessary follow-up.

In summary, Consett is an example of what a well organised, low budget development agency can do to alleviate the worst effects of industrial contraction over a <u>limited</u> area. To classify it as successful requires us to overlook the fact that it has done no

more than attract to Derwentside jobs which would have arisen elsewhere. As yet there is no pattern of firms taking root there which would give rise to hope that a new industrial structure, viable for the long term, is in process of creation.

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AREA REPORT 5

SCOTTISH DEVELOPMENT AGENCY

Special Expenditure

The whole of the western half of Scotland, and small patches on the eastern side are Assisted Areas. Large parts of Strathclyde and Fife are Special Development Areas. Livingstone and Glenrothes are new towns where similar benefits are available, while Clydebank additionally is an Enterprise Zone. These areas all receive the highest rates of regional aid available. The Western Isles, virtually the whole of the Highlands Local Authority and a large part of Dumfries and Galloway are classified as Development Areas, ie the middle of the three tiers of assisted area.

In 1982 the Scottish Assisted Areas received just over 25% of all regional assistance for Great Britain, whereas the whole of Scotland accounts for just over 9% of the GB population.

In addition, Scotland enjoys the services of the Highlands and Islands Development Board (see area report 6) and of the Scottish Development Agency (SDA) - statutory bodies which receive funding directly from the Scottish Office, but also channel Regional Aid in Scotland to candidate companies.

The SDA and HIDB are large scale development undertakings compared with those we visited in London, Corby and Consett. The SDA was established in 1975 to concentrate effort on four priorities: small businesses, the encouragement of inward investment, support for new technology, and area projects such as the Glasgow Eastern Area Renewal. It employs 730 staff headquartered in Glasgow.

The SDA's geographical remit is Scotland-wide, although its efforts are less intense in the HIDB area. The SDA owned net assets of just under £290 million in March 1983 - £260 million in property and £30 million in investments - and had income and expenditure of

S.D.A.

£108 million in the year.

The scale of its investment in Scottish industry suggests an operation which verges on <u>dirigisme</u>. The SDA has investments in 677 small businesses and 858 larger companies. It owns 218 industrial sites and 27 million square feet of industrial accommodation. It sanctioned nearly 450 land renewal schemes in the 12 months ending March 1983.

The emphasis of SDA activity is now shifting away from estate management and towards marketing. The principal benefit which the SDA has to offer is the capacity for creating a "single door package". In other words, firms interested in coming to Scotland do not have to troop around to banks, property companies and a host of different government agencies. SDA is particularly anxious to attract in the newer technologies, particularly microelectronics and biotechnology. The Chief Executive of the SDA, Dr Mathewson, is keen to invest in an artificial intelligence institute as well. He felt, however, that there is a shortage of academic infrastructure, and he also noted that it was necessary to get more good financial men among academics so that the latter could be exposed to commercial disciplines.

Not surprisingly, SDA is prickly about rival inward investment promotions in other parts of Great Britian. Dr Mathewson in particular was worried that the DTI Invest in Britain Bureau might want to start restraining the SDA's own overseas promotion activities.

It is not clear what <u>nett</u> benefit the SDA has brought about. The monitoring of jobs obtained has been unsatisfactory, with the result that no useful figures are yet available. The capital cost per job secured works out in the region of £10,000, but such figures are, the SDA feels, rather misleading. Simply creating jobs is not the answer. "What we need are added value jobs". Our view is that even the approximate figure of £10,000 per job may be a serious understatement. The nine urban renewal projects described in the SDA's Annual Report and Accounts suggest that the cost per job for these

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undertakings is in the region of £47,000.

Glasgow Eastern Area Renewal Project (GEAR)

GEAR is the most expensive of the nine SDA area projects. Its public sector budget of £200 million over ten years to 1986 is now expected to be nearer £300 million, and is more than the cost of all the other projects combined. The expenditure of £300 million public funds is expected to have produced private sector inputs of between £150 million and £200 million by the end of the project, at a cost to taxpayers and ratepayers of about £75,000 per acre or nearly £7,000 per resident.

Although GEAR is managed by the SDA, its public funding comes from no fewer than seven sources - Strathclyde Regional Council, Glasgow District Council, Scottish Special Housing Association, Greater Glasgow Health Board, Housing Corporation, Manpower Services Commission, and Scottish Development Agency itself.

The scale of the problem to be tackled is appalling. Population in the 4,000 acres of Glasgow's East End has fallen from 115,000 to 45,000 since the last war, and the area has become largely derelict. There was a concentration of industrial chemical pollution in the area. Educational standards there are minimal. The aims of the GEAR project are to retain and create jobs, to improve the quality of life and the environment, to create better housing, and to "involve the community". Some of these aims are intangible, which makes measuring success impossible. But even where specific targets could have been set, none has been - a familiar tale.

Richard Colwell, the SDA's Director of Area Projects, said that once the GEAR project has been completed it would be time to turn to the newly emerging black spots in the suburbs. Glasgow has four of these, each with a population of 40,000-50,000, each with dreadful housing. "We need to get there before the decline becomes as bad as it had been in the East End area." Yet, if expenditure to date on GEAR is any guide, we <u>must</u> set clear targets before embarking on any of these further projects.

The GEAR project fully recognises the importance of land assembly and development as the key to urban renewal, and we can only applaud that. What is less clear is the SDA's role, longer-term, in the developed area. It should want to hand over to the private sector, in the manner of the Development Corporations in London and Liverpool; but we suspect that the area will continue to form part of the Agency's ever expanding portfolio of property and industrial investments.

AREA REPORT 6 HIGHLANDS AND ISLANDS DEVELOPMENT BOARD, INVERNESS

The Highlands and Islands Development Board covers a large area of remoter mainland Scotland (roughly the area north and west of a line joining Arran and Elgin) and the surrounding islands. The Board was established in 1965 "for the purpose of assisting the people of the Highlands and Islands to improve their economic and social conditions and of enabling the Highlands and Islands to play a more effective part in the economic and social development of the nation". What this means in action terms is unclear. As the Board itself says, in its 1982 Report, "the Board's remit to develop the area economically and socially is a very wide one and does not in itself help to identify a plan of action ... in publishing our strategic plan we seek only to show the activities on which we are placing importance at the present time." (!)

Like the SDA, the HIDB has and uses powers of investment in companies and projects, and of ownership of land. On its own smaller scale, it is no less dirigiste than the SDA.

The retention of population and the maintenance of incomes evidently figures as a high priority, and the favourite mechanism is industrial investment. As to population, in the 40 years to 1961, the number of people living in the HIDB area fell by nearly 20%, but in the 20 years since then the population has grown again by 16% to 350,000. In 1982, the unemployment rate, at 14.1%, was a little lower than for Scotland as a whole but a little above that for Great Britain as a whole. But long term unemployment was lower, at 28% of unemployed, versus 35/36% for Great Britain and Scotland.

HIDB.

In the ten years to the end of 1982, HIDB assistance at constant 1982 prices totalled £159 million. The corresponding contribution from the private sector was £258 million and overall gearing of 1.6:1 although in 1982 the contribution from private sources had produced a ratio of almost 2.5:1 the best the Board had achieved in the past five years. HIDB estimates that this investment has created

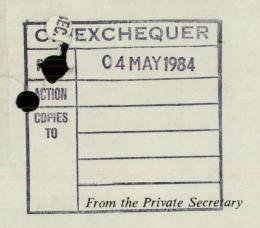
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or retained more than 22,000 jobs at a capital cost, crudely measured, of £7,200 per job. By the end of 1982 the Board owned assets of £47 million, split roughly half and half between land or property and investments in companies. Its expenditure in the year was about £15 million.

Financial support gravitates naturally towards industry sectors already present in the HIDB area: fishing, timber, off-shore rig construction, woollen goods and tourism. There is no specific policy of attracting in novel sectors to the area, although reports have recently been commissioned on the prospects for biotechnology and health care industries in the HIDB area. The scale of new employment opportunities open to HIDB is clearly inadequate to cope with major industrial closures - the pulp mill at Fort William, the aluminium smelter at Invergordon and the threatening shortage of rig work at Highland Fabricators in Nigg Bay.

Even though job creation is a prime objective of the Board, the monitoring of jobs created is not as good as it should be. After five years, the Board takes firms it has assisted off its books because it would be "too time-consuming to keep in touch with every guest house, fish farm and boat". There is, however, an annual audit of jobs in Board factories.

It is not clear that the underlying objectives of maintaining a certain size of population or of maintaining a certain level of average income are in themselves worthwhile. Is it actually undesirable that sparsely populated areas become somewhat more sparsely populated? Does the maintenance of a population by subsidy not tend to generate demands for yet more subsidy, for instance on infrastructure projects? Members of the HIDB were certainly keen to have better telecommunication and more roads like the A9 highway to Inverness. As a political cosmetic, however, we have to rate the activities of HIDB highly. Expenditure of as little as £15 million per annum on such a large geographical area is valuable, if only because withdrawing it could send worrying signals to the more southerly, more heavily populated regions of Scotland.





4 May, 1984.

Employment

Further to Andrew Turnbull's letter of 27 March regarding the Prime Minister's meeting on Friday, 25 May, I am now writing to confirm the arrangements.

This meeting will take place at No.10 and will start at 0930 and finish at approximately 1230. It will not include lunch. An agenda will be circulated shortly.

I am copying this letter to David Peretz (IIM Treasury), Michael Reidy (Department of Energy), John Ballard (Department of the Environment), Elizabeth Hodkinson (Department of Education and Science), Callum McCarthy (Department of Trade and Industry), Alex Galloway (Chancellor of the Duchy of Lancaster's Office), and to Mr. David Young and Sir Robert Armstrong.

Caroline Ryder

David Normington, Esq., Department of Employment.



10 DOWNING STREET

9/5"
AGENDA

From the Private Secretary

9 May 1984

Dees David,

Seminar on Industry and Employment

Caroline Ryder's letter of 4 May (which we requested should be held in private offices) confirmed that there will be a meeting on 25 May at 0930 - 1230. The likely agenda will be:

- (i) Two papers by the Secretary of State for Employment on trends in the labour market and employment prospects; and the impact of Government policies to date and the options for further action.
- (ii) A paper by the Secretary of State for Trade and Industry on how the UK's export promotion effort could be made more effective.
- (iii) A paper by the No 10 Policy Unit on promoting wider ownership of property and financial assets.

There may also be time for members of the group to report orally on items outstanding from earlier meetings. Finally, the Prime Minister may invite colleagues to offer papers for a further meeting after the summer recess.

At the meeting in December, the Policy Unit were asked to compile a dossier of examples of successful enterpreneurship in the regions, identifying the factors behind their success. This they have now done and a copy of their report is enclosed for information.

I would be grateful if you could ensure that this letter could be shown only to Ministers and Principal Private Secretaries and that it is not copied or circulated outside private offices. In commissioning any briefing for this meeting, you should do so without referring to the meeting or its agenda.

I am copying this letter to David Nomington (D/Employment), Michael Reidy (D/Energy), John Ballard (D/Environment), Elizabeth Hodkinson (DES), Callum McCarthy (DTI), Alex Galloway (CDL's office), David Young (MSC) and Richard Hatfield (Cabinet Office).

Your smeets

Andrew Turnbull

David Peretz Esq HM Treasury

relightly relight relightly relightly relightly relightly to the property of t Policy bank asled as to report as bailgrand to the PM's dennia a Friday. Mr Filge does is know its purpose. are you lasty For it to be Lent? It should go acon an Mady. 17/5 The naterial on Mr Shor was apparently regrested separately. To anoid around suspicions lest, I think we can simply beaun delete in his Context.

FROM: M T FOLGER DATE: 15 May 1984

(anni 17/5)

PRINCIPAL PRIVATE SECRETARY -12/2

cc PS/Financial Secretary
Mr Battishill
Mr Allen
Mr Grimstone
Mr Makeham
PS/IR
Mrs S Ayling IR
Mr Lewis IR
Mr Lord
Mr Portillo
Mr Ridley
HF/01

ENCOURAGEMENT OF EMPLOYEE, AND WIDER, SHARE OWNERSHIP

You asked me to co-ordinate preparation of some material about the record on this since 1979. I now attach two notes which between them cover the field:

Note 1 prepared by the Revenue on general measures to encourage employees and wider share ownership.

Note 2, prepared by PE2, on measures to encourage employee and small investors to take up equity in privatisations.

- 2. I also attach a draft letter to No.10.
- 3. I copy all this to Mr Makeham in case the material may be of use in preparing the FST's 3 October speech to the Wider share Ownership Council, or indeed more generally.

M T FOLGER

EX.449 15 /5

UNCLASSIFIED COVERING CONFIDENTIAL

DRAFT LETTER FOR YOUR SIGNATURE

Wite to:
John Reduced

A Turnbull Esq
10 Downing Street
LONDON SW1

ENCOURAGING EMPLOYEE AND WIDER SHARE OWNERSHIP

I attach notes, prepared by Inland Revenue and the Treasury, on relevant measures adopted since 1979. Included at Annex C to the first note is some material on Mr Shore's intervention in the House on 2 May regarding disposals of employee shareholdings.

2. Some of the individual measures in the tax field are quite complicated and are set out only in summary form below. No doubt you will let me know if more detail would be helpful.

D L C PERETZ Principal Private Secretary.

TAX AND OTHER LEGISLATION DESIGNED TO ENCOURAGE EMPLOYEE SHARE OWNERSHIP AND WIDER SHARE OWNERSHIP MORE GENERALLY

A. EMPLOYEE SHARE OWNERSHIP

(Annex A gives figures)

1. Profit Sharing

The reliefs available under the Finance Act 1978 for approved all-employee schemes were made more generous in 1980, 1982 and 1983. Annual limit on value of share allocation per employee is now £1250 or 10 per cent of salary (subject to a ceiling of £5000) compared to £500 in 1979. Minimum retention period for employee shareholdings to attract most favourable tax treatment is now 7 years compared to 10 years.

2. Share Option Reliefs

A new relief was introduced in 1980 for approved all-employee SAYE-linked share option schemes. In 1982 a 3-year instalment relief was provided to spread payment of income tax arising on share options exercised outside these approved schemes - typically by senior managers.

The 1984 Finance Bill:

- (a) increases the monthly savings limit under the SAYE-linked schemes from £50 to £100;
- (b) extends to 5 years the instalment relief for unapproved options granted before 6 April 1984; and
- (c) introduces from 6 April 1984 a new relief for share options granted under schemes satisfying various conditions to qualify for Inland Revenue approval, the usual income tax charge on exercise of the option being replaced by CGT liability on disposal of shares.

3. Employment Act 1982

Companies with over 250 employees required to make an annual statement about employee involvement arrangements, including financial participation.

Interest Relief

Section 24 Finance Act 1983 provides relief for interest paid on loans taken out by employees to buy shares in their employee - controlled company as part of an employee buy-out. Other measures have been introduced to improve the relief available to people investing in their business: close companies (1982), co-operatives (1981) and partnerships (1981).

B. MEASURES ENCOURAGING WIDER EQUITY INVESTMENT GENERALLY

5. Stamp Duty

The cut in the rate of stamp duty to 1 per cent, announced in the 1984 Budget from the 2 per cent rate imposed by the Labour Government in 1974 removes an important disincentive to investment in equities. The reduction in the rate of duty on share transfers should encourage direct share ownership by individuals as well as institutions.

6. Capital Taxation Generally

Capital taxation has been reduced to encourage investment and enterprise. Since 1979:

- (a) the CGT threshold has been increased from £1,000 to £5,600;
- (b) the CTT threshold stands at more than double its 1979 level, (£64,000 rather than £25,000) and the cumulation period has been cut to 10 years. This is of particular value to family firms;
- (c) top rates of CTT cut from 75 per cent to 60 per cent (transfers on death) and

 30 per cent (lifetime transfers). Again this helps family firms;
 - (d) an <u>indexation</u> allowance introduced for CGT, and CTT rate-bands index-linked.

7. Investment Income Surcharge

The investment income surcharge (chargeable for 1983-84 at 15 per cent on an individual's investment income in excess of £7,100) has been abolished with effect from 1984-85. The surcharge was a factor in discouraging individuals from saving or investing directly, in particular in equities, and abolition therefore removes one element of discrimination against direct investment. A total of some 280,000 taxpayers will benefit, at a cost of about £360 million in a full year.

8. Abolition of Life Assurance Premium Relief (LAPR)

The 1984 Finance Bill proposes to abolish LAPR on life assurance contracts made after 13 March 1984 (and existing ones, if subsequently enhanced). This will reduce the fiscal

tortions which favoured investment in life assurance and, together with other tax reform measures, should remove biases which encouraged individuals to invest in institutions rather than directly in equities.

9. Venture Capital Scheme

This was introduced in 1980 to encourage the flow of risk capital into small businesses. It enables investment companies, as well as individuals, to set losses from investments in unquoted shares against income instead of capital gains, thereby enhancing the value of the loss for tax purposes. Thus the relief offers reassurance to those who provide risk capital by sharing with them any loss on the failure of their investment.

10. Business Expansion Scheme

The BES was introduced in 1983 and greatly extended and improved the 1981 Business Start-Up Scheme. It is an unprecedented measure, more closely targetted but also far more generous than, for example, the Loi Monory. It offers income tax relief at full marginal rates on up to £40,000 a year to encourage individual outsiders to invest in the full-risk ordinary shares of new and expanding unquoted trading companies.

11. Purchase of Own Shares

The 1982 Finance Act eased the tax charge when unquoted companies buy back their own shares to the benefit of their trade. This encourages more equity investment because owners and investors are often understandably concerned about finding a way out. Thus, for example small companies should be encouraged to set up employee share schemes since with a buy-back provision their shares are more readily marketable. The measure can also assist "management buy-outs" - the managers purchasing a small number of shares and the company buying back (and cancelling) the balance held by existing shareholders.

INLAND REVENUE
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ANNEX A to Note 1

TAKE-UP OF EMPLOYEE SHARE SCHEMES

- 1. By 30 April 1984 the total number of <u>schemes</u> qualifying for tax relief was 689 (397 Finance Act 1978 profit sharing and 292 Finance Act 1980 savings-related share option schemes). Compares with less than 30 approved schemes in 1979 when Government took office. No reliable figures for unapproved share option schemes but estimated there may be around 1000.
- 2. Number of approved schemes considerably understates number of <u>companies</u> since many schemes cover group of companies. No precise figures of total numbers but estimated that there are currently approaching 2000 companies participating in profit sharing schemes and over 45000 in SAYE-linked share option schemes; figures cannot be cumulated as some companies will participate in both but total must certainly be in excess of 5000.
- 3. Estimated that nearly ½ million employees have benefited under approved schemes since 1979 (ie have been allotted shares or given options to buy shares). A 1981 commercial survey estimated that companies employing total of over 1½ million employees had some form of scheme, approved or unapproved.
- 4. <u>In money terms</u> (on basis of estimated figures up to March 1983) employees have been allocated £m195 worth of shares under profit sharing schemes and been granted options under SAYE-linked schemes to value of £350m. No figures available for unapproved schemes.

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Note 2

PRIVATISATIONS: MEASURES TO ENCOURAGE EMPLOYEES AND SMALL INVESTORS TO BUY SHARES

I. EMPLOYEE SHARE OWNERSHIP

1. 1983 Manifesto

The Manifesto stated that in privatising BT, Rolls Royce, BA etc "we will offer shares to all who work in them."

2. Extent of special arrangements for employees

Special arrangements have been made to encourage employee participation in all privatisations where a majority shareholding has been sold by stockmarket flotation.

3. Typical pattern of arrangements

Arrangements for employees typically include

- (a) An offer of free shares

 (b) An offer of matching shares given
 free in proprotion to shares
 purchased by the employee

) shares placed in trust for
 at least2 years- see
) Annex C.
- (c) A Special application form which gives the employee priority in the allocation of any shares that he may apply for in addition to the free and matching offers.

[CONFIDENTIAL - NOT FOR DISCLOSURE: Guidelines limiting the value of the elements of an offer were laid down in 1980 as £50 maximum free offer and overall cost of free and matching offers not to exceed an absolute maximum 5 per cent of Gross Proceeds. The Guidelines have been adhered to - allowing for a rise in the free offer broadly in line with inflation.]

4. Exceptions to the typical pattern

British Petroleum, where there was no free offer. The Cable and Wireless privatisation where matching shares were to be made available over a period as part of the companies employee profit sharing scheme. The British Telecom scheme, which will include a discount on shares applied for in addition to the free and matching offers.

The National Freight Corporation was an employee/management buyout.

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5. Arrangements during subsequent sale of any residual Government shareholding

No free or matching shares have been provided by the Government but special application forms have been distributed giving priority to employees in allocation.

6. Details of arrangements in individual cases

A table is attached at annex A giving brief details of each relevant privatisation.

7. Bull points on success of arrangements for employees

Around 90 per cent of eligible employees have participated in the schemes to date with about 100,000 becoming shareholders in their own companies.

8. Mr Shore's charge that employee shareholdings are quickly sold

Attached at Annex C is a note, with a line to take, on erroneous remarks by Mr Shore on the occasion of the Secretary of State's 2 May on BT privatisation.

II OTHER SMALL INVESTORS IN PRIVATISATIONS

9. The Financial Secretary replied to a question from Mr Tony Banks (Hansard 23 February 1984 W.A Col 590) in these terms:

"It is our policy to encourage participation by private individuals in individual share sales wherever this is appropriate".

10 Arrangements for small investors

Arrangements to encourage applications by small investors have included:

- (a) Wide advertisement of sale and broad distribution of prospectus.
- (b) Preferential treatment in allocation.
- (c) Opportunity to apply at the striking price in tender offers (thus helping inexperienced investors by removing the need for them to judge a price to bid).

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(d) In one case (Britoil) a loyalty bonus with free shares given in proportion to those held for a minimum period after the sale.

[CONFIDENTIAL - NOT FOR DISCLOSURE: items (b) and (c) are essentially costless but item (d) represents a discount, delayed in time, on the price of shares. This discount may be offset by increased demand, but because of uncertainty over possible net cost there is no firm commitment to use this technique in the generality of sales.]

11. Details of arrangements in individual cases

A table is attached at annex B giving brief details of each relevant privatisation.

PE2 H M Treasury May 1984

EMPLOYEE SHARE SCHEMES IN PRIVATISATIONS

1. Summary of Key Figures

Company (Date of Sale)	Maximum Value* of Incentives Per Employee	Percentage [†] of workforce participating	Percentage [†] of Issued Share Capital Held
	£	£	£
BP (October 1979)	500	43	0.25
British Aerospace (February 1981)	499	74	3.6
Cable and Wireless (October 1981)	300	99	1.4
Amersham International (February 1982)	550	99	3.7
National Freight Company (February 1982)	£200interest free loan for share purchase	23 ^ø	82.5
Britoil (November 1982)	458	72	0.1
Associated British Ports (February 1983)	311	91	4.3
British Telecom (announced arrangements)	470	N/A	N/A

^{*}Maximum value of shares available free to an employee under both free and matching offers plus value of any other financial incentive.

⁺Initially following sale.

 $[\]phi_{\text{Percentage of employees and pensioners involved.}}$

ANNEX A to note 2

EMPLOYEE SHARE SCHEMES IN PRIVATISATIONS (cont)

2. Outline of Schemes*

2. Outline of schemes			
Company (Date of Sale	Free [†] Offer	Matching ⁰ Offer (Free: bought)	Other Financial Incentives
BP (October 1979)	None	Max £500 (1:1)	None
British Aerospace (February 1981)	£49.50	Max £450 (1:1)	None
Cable and Wireless (October 1981)	£50.00	£250 ⁺ (1:1)	None
Amersham International (February 1982)	£50.00	Max £500 (1:1)	None
National Freight Company (February 1982)	(Management/E	Employee Buyout)	£200 interest free loans
Britoil (November 1982)	£58.50	Max £400 (1:1)	None
Associated British Ports (February 1983)	£59.33	Max £252 (1:1)	None
British Telecom (announced arrangements)	£70.00	Max £200 (2:1)	10 per cent discount on up to £2000 of further shares

^{*} All schemes include preferential application forms for further shares which give employees priority in allocation.

Value of shares at time of privatisation which HMG was to make available over the life of the Company's profit sharing scheme.

⁺ At offer price.

O By HMG or company Trust.

Annex A to Note 2

EMPLOYEE SHARE SCHEMES IN PRIVATISATIONS (cont)

3. Take up of Offers (per cent eligible employees)

Company (Date of Sale)	Free Offer	Matching Offer	Preferential Application Forms
BP (October 1979)	N/A	50	53
British Aerospace* (February 1981)	89	41	1.6
Cable and Wireless* (October 1981)	99	99	25
Amersham International* (February 1982)	99	80	40
National Freight Company (February 1982)	(23% of employees and pensioners participated in the Management/Employee Buyout)		
Britoil (November 1982)	92	62	not available
Associated British Ports (February 1983)	90	38	2.9
British Telecom (announced arrangements)	N/A	N/A	N/A

^{*} Average employee holding estimates as: BAe £161, Cable and Wireless £585, Amersham International £1,680.

⁺ Directors, Employees, Employees, Immediate families, Pensioners formlery employed by the company, their wives and or widows/widowers were all eligible.

ANNEX A

EMPLOYEE SHARE SCHEMES IN PRIVATISATIONS (cont)

4. Number and Value of Shares Involved

Company (Date of Sale)	Number of Shares Applied For	Number of Shares Allocated	Per cent Share* Capital Held
BP (October 1979)	Not available	Not available	0.25
British Aerospace (February 1981)	10,612,008	7,072,300	3.6
Cable and Wireless (October 1981)	3,785,833	3,785,833	1.4
Amersham International (February 1982)	2,014,140	1,828,290	3.7
National Freight Company (February 1982)	6,187,500	6,187,500	82.5
Britoil (november 1982)	580,610	580,610	0.1
Associated British Ports (February 1983)	1,856,875	1,736,965	4.3
British Telecom (announced arrangements)	N/A	N/A	N/A

^{*} Issued share capital held by employees immediately following sale.

ANNEX B to note 2

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ARRANGEMENTS FOR SMALL INVESTORS IN PRIVATISATIONS

Company (Date of Issue)	Distribution* of Prospectus	Preference in Allocation	Any other measures
BP (October 1979	Post Offices, Shareholders Clearing Banks, Co-op Bank, TSB's	Yes	
British Aerospace (Feburary 1981)	Main branches Lloyds, Clydesdale Bank, Bank of Ireland	Yes	
Cable and Wireless (October 1981)	Main branches Natwest, Ulster Bank, Hong Kong	Yes	
Amersham International (February 1982)	Regional Stock Exchanges	Yes	-
Britoil (November 1982)	Post Offices, Clearing Banks, TSB's	Offer by Tender	Striking price applications 1 for 10 loyalty Swall bonus (after 3 years)
Associated British Ports (February 1983)	Lloyds branches, Bank of Ireland	No	-
BP (SeptemberC1983 ⁺	Main branches of several UK Banks, Main Post Offices	Offer by Tender	Striking price Applications
Associated British Ports (April 1984 ⁺	All branches of Lloyds Bank, Bank of Ireland	Offer by Tender	Striking price Applications

^{*} Other than to Bank of England, Merchant Banks, Underwriters, Brokers and Receiving Banks.

⁺ Sales of residual holdings.

Annex C to note 2

MR SHORE'S STATEMENT (OR 2 MAY COL 354) THAT EMPLOYEES SELL SHARES QUICKLY

"... Previous attempts to make privatisation popular by dispersing shares to existing employees have resulted in about 84 per cent of all such allocations being disposed of by the recipients within one week of becoming the owners".

1. Background

[CONFIDENTIAL: NOT FOR DISCLOSURE: Free and matching shares allocated to employees in privatisations are placed in trust for a minimum of two years and may not be sold or pledged as security during that period except in case of injury, disability, redundancy or retirement. Beyond this there is a further period up to seven years from allocation when the shares may be traded at the cost of losing some or all of their tax exemption. Although we do not have figures, since a large proportion are in trust, it is highly unlikely that Mr Shore's statement is true. He is almost certainly confusing employee shareholders with the generality of small investors. There is some evidence of falls of this magnitude in the holdings of other small investors. (For example, in the case of British Aerospace, excluding employees, shareholders holding less than 1000 shares fell by 84 per cent in just under one year. This is probably the source of Mr Shore's figure. There was a similar fall in the case of the 1981 Cable and Wireless sale). How much of this is due to professional stock market speculators ('stagging' the offer) and how much to ordinary investors taking profits or otherwise adjusting their portfolios after allocation we cannot tell. The loyalty bonus in the case of Britoil was designed to combat the professional speculator. Initial evidence shows small shareholdings holding up well - but then Britoil was heavily under-subscribed with a poor aftermarket. In general, widespread selling immediately after an offer is only likely to be a problem in fixed price offers which prove to be underpriced.]

Suggested line to take

(a) 84 per cent Fall in Employee Shareholdings?

"It is the Government's intention to encourage long term participation by employees in their company and indeed free shares are usually held in trust for their owners for a minimum period. I am therefore surprised that the hon gentleman should feel able to state that 84 per cent of the employees holding are sold within a week. I should like to see his evidence."

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(b)

84 per cent Fall in Small Investors Holdings?

"The fact that large numbers of small investors have been involved in privatisations to date is a tribute to the Government's policy of encouraging their applications. It is not unusual for there to be a high turnover in shares in the period immediately following a flotation but I have seen no evidence to suggest that recent privatisations have particularly suffered from this."

No 10
Policy
UNIT ON
WIDER
OWNER

WIDER OWNERSHIP

17 May 1984 Policy Unit

The Conservative Manifesto states:

"A free and independent society is one in which the ownership of property is spread as widely as possible. A business which is partly or wholly owned by its workers will have more pride in performance. . .

"Under this Government, the property-owning democracy is growing fast. And the basic foundation of it is the family home."

"We want to encourage wider ownership. This means lowering taxes on capital and savings; encouraging individuals to invest directly in company shares; and encouraging the creation of more employee share schemes."

Why is the private ownership of property so important to a free society?

The home-owner has many freedoms which council tenants do not enjoy. He can move anywhere in the country by selling his house and buying a new one; he can improve, renovate and paint his house as he sees fit, subject to planning controls; he can borrow against his assets and use profits from sale for other purposes. This can help him finance enterprise and business ownership.

The shareholder and part-owner of a business has rights which an ordinary employee or customer does not have. True employee involvement in company affairs comes through share-ownership. He can make his views known on the future direction of the company, its policy, its management and style. He can vote on board policy, and to support or reject the candidatures of directors.

In summary, the ownership of property brings people new rights. It spreads power in the community. It brings new responsibilities. The home-owner has to repair his own property. The employee-shareholder thinks about the profitability of the company as well as about his next wage claim. It is the best bulwark against nationalisation and confiscation of assets by the state. People gain a vested interest in freedom. Wider ownership can ward off negligent management, or the abuse of power in large companies. Wider share-ownership enables others to participate in the profits of hi-tec and rising productivity. Home-ownership removes the threat of tyrannical landlords - whether they be council or private.

A policy of wider ownership is both popular and stable. Policies to enforce redistribution of wealth become so much less attractive when wealth is more widely spread. It is

one of those few examples of a policy which, at one and the same time, meets with very widespread support and is extremely difficult to reverse.

What are the options for stimulating home-ownership further?

Home-ownership is now a realistic objective for two-thirds of the population, and over 60 per cent have now achieved this aim. It could easily become reality for three-quarters of the population. Some of the better council housing estates are already being transformed by their new owners keen to renovate their homes, improve their gardens and change the face of their estate.

a. The functioning of the housing market. For some buyers, particularly first-time buyers, the costs and complexity of house purchase can still represent a serious obstacle. The Government has started to take action, halving Stamp Duty, raising the threshold, and announcing an investigation into the solicitors' conveyancing monopoly.

Stamp Duty and legal costs remain large expenses in the purchase of a home. The options therefore include:

- i. a further reduction in Stamp Duty (threshold and/or rate);
- ii. ensuring that enough competition is introduced into the provision of conveyancing services to lower the cost and improve the quality of the service (Committee now investigating how to proceed);



- iii. a more rapid extension of registered land, which is the best way of cutting the costs and complexity of securing a recognised title;
- iv. further encouragement of competition between
 estate agents, who are now beginning to compete
 on fee as well as on service. {E(CP) could
 look at this question.}
- b. Council house sales.
 - i. The Right to Buy scheme can be extended to include the right to buy houses on leasehold land and the right to buy on a shared-ownership basis (Manifesto pledge). Housing and Building Control Bill is proceeding along these lines.

PX

ii.

The maximum discount can be increased further. Housing and Building Control Bill raises it to 60 per cent after 30 years.

pX

- iii. The period during which the house has to be held in order to gain the exemption from any clawback of the discount could be reduced from the current 5 years.
- iv. More publicity could be given to the schemes. Something is planned for September by the DoE, which could include leaflets, adverts and building society help.
- v. The question of obstructive and dilatory councils could be re-examined. The Secretary of State does have powers to intervene under the 1980 Act.
- c. Encouraging more private sector owners. The best way of encouraging home-ownership is the encouragement of a low interest rate policy through tight control of public borrowing, in accordance with the general economic strategy. Tony Crosland remarked as Housing Minister that he eventually discovered that the Chancellor ran housing policy! Options here include:
 - i. A renewed drive to sell the vacant land owned by local councils, nationalised industries and health authorities, particularly in urban areas, in a concerted effort to get more, cheaper, developable land available for the construction of low-cost homes. Such a drive in docklands has already led to the construction of homes in the £25-35,000 range, which brings them within the reach of many people who never dreamt they could afford a home anywhere near the centre of London. NHS vacant residential accommodation could also be sold.
 - ii. A renewed drive to develop homesteading schemes to move people in to derelict property, often owned by councils, which they can then rehabilitate in return for favourable terms on rent with an option to purchase. There are far too many tinned up terrace houses that should be used.
- iii. Encouragement of building and improvement for sale by local authorities. This can involve

using public wasteland through partnership schemes.

- iv. Careful drafting of the building society legislation to enable them to strengthen the services they provide in the housing market, without allowing them powers to lend money for industrial purposes.
- v. Allocating more money to the Housing
 Corporation to facilitate do-it-yourself
 shared ownership.

What can be done to encourage employee shareholdings more fully?

Continuing the policies to reward enterprise, so that people can make money by owning shares in a profitable business is the best way of proceeding. Lower taxes are the main necessity, coupled with a stable economy so that equity values are not subject to violent downward adjustments.

Some of the options before the Government are:

- 1. Making the Enterprise Allowance scheme demanddetermined at the expense of some of the most costly job-creation programmes. (Under consideration.)
- 2. Continuing to offer a wide range of incentives to employees to buy shares in denationalised concerns. The three main techniques are the free offer of shares to all employees; the offer of additional shares at a discount to the public price, with some limitations on the number; and the pink-form preferential applications for shares in the issue at the public price. All these three techniques have worked in the past, and should continue to be a predominant feature of those denationalisations not being handled by management buy-out. (See DTI paper.)
- 3. A revised fiscal regime for all savings (see below) to make direct ownership at least as attractive as, and preferably more attractive than, institutional ownership.

Why is wealth largely held through institutions?

Institutional ownership of company securities has built up rapidly over the last 20 years. There are now estimated to be only half a million independent private shareholders in British companies in the UK, even though there are 2 million people with private wealth holdings, apart from their house and their pension fund, in excess of £10,000.

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The aggregate figures for the personal sector wealth holdings in September 1983 were:

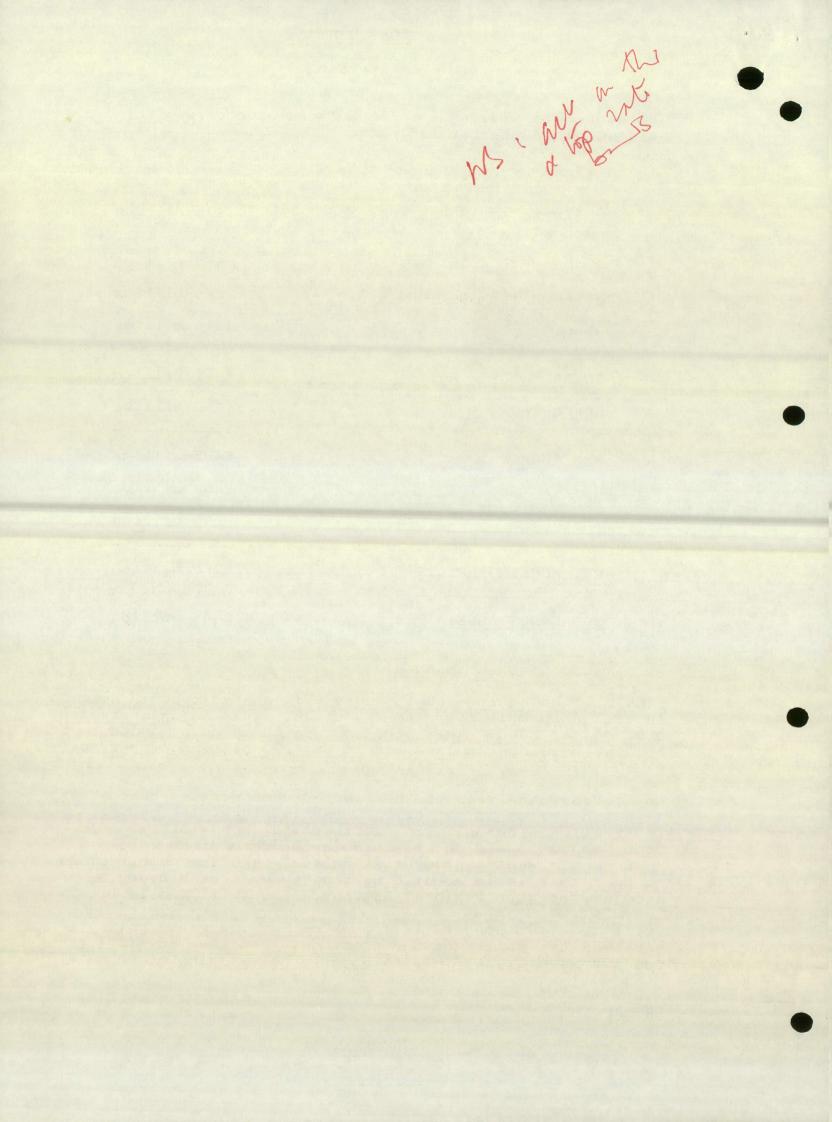
Insurance and pension fund investments	£175	billion
Building society shares and deposits	£75	billion
Company securities	£55	billion
National Savings and gilts	£45	billion
Others	£40	billion
TOTAL	£455	billion
Borrowings	£50	billion
NET ASSETS	£405	billion
Houses (end 1982)	£350	billion
Mortgages	£90	billion
NET HOUSING ASSETS	£260	billion
TOTAL NET ASSETS	£665	billion

(CSO figures rounded)

£405 billion of non-housing assets is shared roughly between 40 million people over the age of 18. This is an average of £10,000 per head. This stock of wealth is being added to by regular saving. In 1982, there was £20 billion of personal saving; in 1983, £17 billion.

Any cursory analysis of the figures demonstrates that a very high proportion is either held cautiously or through institutional hands. The odd thousand pounds or two held by most people should not be held in the form of shareholdings. Most people want a prudential balance, and a sensible place to keep that is in a building society or a bank deposit account, or with National Savings. This will remain true.

Until the last Budget, if I took out an insurance policy I received tax relief on the premiums. And even now if I take one out as a higher-rate taxpayer, the taxation of the



income on the investment is sheltered by the 37.5 per cent insurance company tax rate, compared with the 60 per cent if paying top rate tax. If I buy a house, the interest on the mortgage can be offset against tax, and the asset is free of capital gains on disposal. If I wish to save for my retirement through an institutionalised pension fund, I receive tax relief on the contribution, on the investment and capital gain within the fund, and on the lump sum which I can get in part payment on retirement. If I invest up to a given sum in National Savings, SAYE and a Girobank account, I get tax relief on the interest paid. And if I buy a Government security and hold it for longer than 1 year, I am exempted from Capital Gains Tax. If, however, I choose to go out into the marketplace and buy an ordinary share in a British company, I get no tax relief whatsoever.

There are two ways of approaching this difficulty. One way is to give some limited tax relief to encourage direct investment in shares along the lines of the Loi Monory in France. The alternative way is to tackle the problem of the incentives to institutional saving. The Government has started out on this latter course to simplify tax. It is assumed, for the purposes of this paper, that this is the right route and it is the one that the Government will want to pursue.

The big areas to examine are pensions and life insurance.

Pensions. The average member of the average pension scheme has £11,000 of assets about which he knows little. Norman Fowler's Inquiry into pensions is making progress in finding ways in which people can be sure that they will get a realistic transfer value from their pension scheme when they leave; and in finding ways in which those individuals who wish to be more personally associated with this part of their wealth can do so. Policies to force more disclosure of what the individual is worth, to force better transfer values, and to give a wider range of options to those joining companies or moving companies or setting up in business on their own, are all methods for moving towards a world in which individuals understand this enormous wealth that they own and have more direct control over it.

Another option is to consider breaking some of the fiscal advantages enjoyed by the pension funds.

Insurance company investments. The removal of life assurance premium relief is likely to make a considerable impact on the number of new insurance policies sold. Many of these polices had become an elaborate method for capturing tax relief for

LASAAZ

investment schemes, whereas the original intention was to encourage life cover. The market will now concentrate on selling pension schemes instead of life assurance-related savings.

Making markets more accessible to individuals. In addition to the fiscal advantages of institutional ownership, to the average man the stock market is a remote rich-man's casino, and he would not know how to go about buying a share even if he wanted to.

He is put off by:

- (a) The absence of retail outlets in the average high street the building societies only grew like Topsy as and when they were able to install attractive looking branches in every town and shopping high street in the land.
- (b) The high costs of dealing 1 per cent contract stamp, coupled with 1.65 per cent stockbroker's commission and a 3-4 per cent jobber's spread.
- (c) Attitudes of much of the financial community who have not been actively encouraging the small man to use their services.
- (d) Fears of losses or of being caught up with wrong advice.

Many of these problems can and should be tackled by the impending revolution in the City. One of the changes that should take place is the development of retail branches transacting share business. The building societies on an agency basis, the Post Offices, the major clearing banks, even some of the large chain stores all have the outlets which could offer this facility. It may be that firms like the new Charterhouse-Hambro merger will take the lead. Another developing route will be purchase through TV/home computer telephone-linked services direct to your home.

Dealing costs have been reduced by the halving of Stamp Duty in the Budget. As the market moves towards a new trading system, based on an amalgamation of jobbing and broking, the spreads and commission costs of dealing particularly in the larger shares should come down quite sharply. Whether they will do so for the small man or not depends on whether "execution houses" spread in the UK as they have in the US, offering a cheap, no-frills business to all comers. It is desirable that they should.

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Nothing succeeds like success. If people do start buying shares and they go up in value, they will become shareholders for life. Governments cannot legislate for rising markets, but they can try to pursue economic policies that favour profits and dividend growth (as with the corporate tax changes) and offer a stable environment for business. As the veils are removed on pension fund values and assets, more and more people will come to appreciate that their futures are already ventured in Stock Exchange securities, and some will want more direct control or choice over adviser.

Much of this is a chicken-and-egg question. Many people in the City say of course they would do the business if the business were there to do; whilst others object that the business will not be there to do unless they show they are willing and happy to do it in a friendly and efficient way. The Government should give every encouragement to the development of a retail Stock Exchange, and should certainly eschew regulation of the market in a way which bolsters the role of the big institutions at the expense of the small man. It can encourage full disclosure of dealing, oppose cartels, and show people what they own through its pension, insurance and building society policies and legislation.

CONCLUSION

Wider property-ownership is central to the philosophy of this Government, is politically popular, and is difficult to reverse.

It can be given renewed impetus by:

- (a) A further stimulus to council house sales.
- (b) Policies to associate people with their pension fund wealth more directly.
- (c) Fiscal neutrality between savings mechanisms.
- (d) Using the changing shape of the City to expose individual wealth, and regulating and legislating in a way which encourages individuals to participate.
- (e) The denationalisation programme. BT is an especial opportunity to widen share-ownership in view of its size and the publicity planned for it.

ANNEX

What action has the Government taken to increase home-ownership?

The Government has been successful in encouraging more people to own their own home. In Great Britain in December 1961, there were 7,085,000 privately-owned homes. This figure had risen to 9,598,000 by December 1971; to 11,430,000 by April 1979; and now stands - at the end of 1983 - at 12,900,000. This process has been assisted by:

- A system of mortgage interest relief against income tax, which makes investment in housing a most attractive proposition.
- 2. Exemption of a house, if it is the owner's main residence, from Capital Gains Tax.
- 3. The steady growth in capital values of houses.
- 4. The restrictions placed upon building societies from lending money for purposes other than home-buying, coupled with their success in being popular channels for private savings.
- 5. The encouragement of council house sales to tenants at generous discounts.
- 6. The encouragment of sale of derelict land, particularly from the public sector in urban areas, to assist housebuilders wishing to construct cheaper housing.
- 7. The encouragement of a range of low-cost, low-start mortgage schemes and part equity schemes for house-buyers.

LASABC

What is being done to extend employee shareholdings?

The Government is extending the number of employee shareholdings by:

- The Budget reliefs for new employee shareholding schemes.
- 2. Encouraging management buy-outs in the public and private sectors. The National Freight Corporation was a singular success, where the managers and lorry drivers bought up their business and transformed it and are now sitting on profits of over 400 per cent on their stake money.
- 3. Encouraging employee shareholdings when businesses are denationalised through employee preference schemes.
- 4. The range of measures to help small business, and the Enterprise Allowance to encourage people to set up on their own.
- 5. Some moves towards fiscal neutrality to make institutionalised saving less attractive, particularly with the abolition of life assurance premium relief.

LASABD

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ANNEX 2





EMPLOYEE SHARE OWNERSHIP IN PRIVATISATION

Special arrangements have been made to encourage employee participation in all privatisations where a majority shareholding has been sold by stockmarket flotation. Annex A gives brief details for each relevant privatisation.

Typical Pattern of Arrangements

- 2. Arrangements for employees typically include:
 - a) an offer of free shares;
 - b) an offer of matching shares given free in proportion to shares purchased by the employee;
 - c) a special application form which gives the employee priority in the allocation of any shares that he may apply for in addition to the free and matching offers.
- 3. Guidelines limiting the value of the elements of an offer were laid down in 1980 as £50 maximum free offer, and overall cost of free and matching offers not to exceed an absolute maximum 5% of gross proceeds. The Guidelines have been adhered to allowing for a rise in the free offer broadly in line with inflation.
- 4. Free and matching shares allocated to employees in privatisations are placed in trust for a minimum of two years and may not be sold or pledged as security during that period except in case of injury, disability, redundancy or retirement. Beyond this there is a further period up to seven years from allocation when the shares may be traded at the cost of losing some or all of their tax exemption.

Exceptions to the Typical Pattern

British Petroleum, where there was no free offer. The Cable and Wireless privatisation where matching shares were to be made available over a period as part of the company's employee profit sharing scheme. The British Telecom scheme, which will also include a discount on shares applied for in addition to the free and matching offers. The National Freight Corporation was an employee/management buy-out.



- 6. The details of the British Telecom arrangements as announced by the Secretary of State in the House of Commons on 2 May are:
 - Employees who work at least 16 hours per week for BT and who have been in continuous employment with BT from April 2 1984 until a date shortly before the flotation will benefit from a special scheme. They will be offered about £70 worth of free shares and for every share purchased by the employee the Government will provide a further two free shares up to a maximum of £200 of free shares for £100 of purchased shares. Employees will therefore have the opportunity to acquire about £370 worth of shares for an investment of about £100. As in past sales these shares will have to be vested in a trust for a minimum of two years.

In addition a discount of 10 per cent off the public offer price will be offered to all employees at the time of flotation on purchases of up to £2,000 worth of shares provided that they are held for a specific period. '

Arrangements during Subsequent Sale of any Residual Government Shareholding

7. No free or matching shares have been provided by the Government but special application forms have been distributed giving priority in allocation.

ENCOURAGEMENT OF SMALL INVESTORS IN PRIVATISATIONS

- 8. Arrangements to encourage applications by small investors (details in Annex B) have included:
 - a) wide advertisement of sale and wide distribution of prospectus outside London;
 - b) small minimum allotment size;
 - c) preferential treatment in allotment by scaling down large applications more than small in oversubscribed flotations or by weighting any ballot in favour of small applications;
 - d) opportunity to apply at the striking price in tender offers (thus helping inexperienced investors by removing the need for them to judge a price to bid).



Exceptional arrangements

9. Britoil, a loyalty bonus with free shares in proportion to those held for a minimum period after the sale. This represents a discount, delayed in time, on the price of the shares, with a view to stimulating demand. British Telecom, special incentives to telephone subscribers (eg vouchers which can be offset against subsequent telephone bills). The British Telecom flotation is by far the largest privatisation.

SUCCESS OF POLICIES

- 10. Annex A shows the percentage of employees participating in privatisation issues and the number of shares allotted to them. Considerable success can be claimed with more than 90% participation in several issues. The intention is to encourage long term investment as illustrated by the minimum period for which free shares are held in trust.
- ll. The various measures to encourage small investor participation have also been successful although here it is less easy to claim that investment has been motivated by long term considerations. Where an issue is successful in the sense of oversubscribed at the issue price it is inevitable that some shareholders will sell out when dealings commence. Institutions will be anxious to buy if the allotment has been biased against them. A large reduction in the number of shareholders after the issue has been characteristic of the oversubscribed flotations as the table below illustrates:

1	Size of Offer (£m)	Times sub- scribed	Issue Price (p)	Price on First Day (p)	No.of Allot- ments (K)	No of Share- holders (Nov 83)
British Aerospace	150	3.5	150	169	158	26.2
Cable and Wireless .	224	5.6	168	197	150	26.1
Amersham Int	71	24.6	142	190	63	7.7
A B Ports .	22	33.7	112	138	37	8.3

The number of shareholders apparently fell by over 80% in the first year in the British Aerospace and Cable and Wireless sales.

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- 12. It is impossible to distinguish profit taking by the more professional 'stags' and the 'ordinary' small investor. The tender method is designed to reduce the scope for stagging (but will not remove it when small applications are allowed at the striking price). But the method is more complicated and in that respect may be less attractive to small investors. Efforts to encourage wider participation by favouring small applications will encourage stags to apply for a large number of small applications (there is no practicable cost effective way of preventing multiple applications).
- 13. Stagging is of course in no way peculiar to Government privatisations.

AHNW A

EMPLOYEE SHARE SCHEMES IN FRIVATISATIONS Summary of Key Figures

Company (Date of Sale)	Maximum Value* of Incentives Per Employee	Percentage+ of workforce participating	Percentage+ of Issued Share Capital Held
BP (October 1979)	£500	43	0.25
British Aerospace (February 1981)	£499	74	3.6
Cable and Wireless (October 1981)	£300	99	1.4
Amersham International (February 1982)	£550	99	3.7
National Freight Company (February 1982)	£200 interest free loan for share purchase	23 ^p	82.5
Britoil (November 1982)	£458	72	0.1
Associated British Ports (February 1983)	£311	91	4.3
British Telecom (announced arrangements)	£470	N/A	N/A

Notes:

- * Maximum value of shares available free to an employee under both free and matching offers plus value of any other financial incentive.
- + Initially following sale.
- * Percentage of employees and pensioners involved.

EMPLOYEE SHARE SCHEMES IN FRIVATIBATIONS

В.	Outline	of	Schemes*	

Company (Date of Sale)	Free † Offer	Matching Offer (Free: -bought)	Other Financial Incentives
BP (October 1979)	None	Max £500 (1:1)	None
British Aerospace (February 1981)	£49.50	Max £450 (1:1)	None
Cable and Wireless (October 1981)	£50.00	£250 (1:1)	None
Amersham International (February 1982)	£50.00	Max £500 (1:1)	None
National Freight Company (February 1982)	(Management/Empl	oyee Buyout)	£200 interest free loans
Britoil (November 1982)	£58.50	Max £400 (1:1)	None
Associated British Ports (February 1983)	£59.33	Max £252 (1:1)	None
British Telecom (announced arrangements)	£70.00	Max £200 (2:1)	10% discount on up to £2000 of further shares

Notes:

- * All schemes include preferential application forms for further shares which give employees priority in allocation.
- Value of shares at time of privatisation which HMG was to make available over the life of the Company's profit sharing scheme.
- At offer price.
- o By HMG or company Trust.

•	C. Take up of Offers (pe			
	Company (Date of Sale)	Free Offer	Matching Offer	Preferential Application Forms
	BP	N/A	50	43
	(October 1979)			
	British Aerospace*	89	41	1.6
	(February 1981)			
	Cable and Wireless*	99	99	25
	(October 1981)			
	Amersham International*	99	80	40
	(February 1982)			
	National Freight Company (February 1982)	(23% of emparticipa Buyout) +	mployees and pensioner ated in the Managemen	rs t/Employee
	Britoil	92	62	not available
	(November 1982)			
•	Associated British Forts (February 1983)	90	38	2.9
	British Telecom	N/A	N/A	N/A

Notes:

(announced arrangements)

- * Average employee holding estimated as: BAe £161, Cable and Wireless £585, Amersham International £1,680.
- + Directors, Employees, Employees, Immediate families, Pensioners formerly employed by the company, their wives and or widows/widowers were all eligible.

EMPLOYEE SHARE SCHEMES IN FRIVATISATIONS D. Number and Value of Shares Involved

Company (Date of Sale)	Number of Shares Applied For	Number of Shares Allocated	% share* Capital Held
BP (October 1979)	Not available	Not available	0.25
British Aerospace (February 1981)	10,612,008	7,072,300	3.6
Cable and Wireless (October 1981)	3,785,833	3,785,833	1.4
Amersham International (February 1982)	2,014,140	1,828,290	3.7
National Freight Company (February 1982)	6,187,500	6,187,500	82.5
Britoil (November 1982)	580,610	580,610	0.1
Associated British Forts (February 1983)	1,856,875	1,736,965	4.3
British Telecom (announced arrangements)	N/A	N/A	N/A

Notes:

^{*} Issued share capital held by employees immediately following sale.

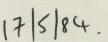
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ARRANGEMENTS FOR SMALL INVESTORS

Company (Date of Issue)	Distribution* of Prospectus	Preference in Allocation	Any other measures
BP (October 1979)	Post Offices, Shareholders, Clearing Banks, Co-op Bank, TSB's	Yes	-
British Aerospace (February 1981)	Main Branches Lloyds, Clydesdale Bank, Bank of Irel and	Yes e	
Cable and Wireless (October 1981)	Main Branches NatwestyUlster Bank, Hong Kong	Yes	-
Amersham International (February 1982)	Regional Stock Exchanges	Yes	-
Britoil (November 1982)	Post Offices, Clearing Banks, TSB's	Offer by Tender	Striking price Applications 1 for 10 loyalty bonus (after
Associated British Ports (February 1983)	Lloyds Branches, Bank of Ireland	No	3 years)
BP (September 1983)	Main Branches of several UK Banks, Main Post Offices	Tender	Striking price Applications
Cable and Wireless (December 1983)	Main Branches of several UK Banks, Main Post Offices	Tender	Striking price Applications
Associated British Ports (April 1984)	AUBranches of Lloyds Bank, Bank of Ireland	Offer by Tender	Striking price Applicat page

Notes

- * Other than to Bank of England, Merchant Banks, Underwriters, Brokers and Receiving Banks.
- + Sales of residual holdings





STEPS TO PROMOTE WIDER SHARE OWNERSHIP

A 1981 survey by the Stock Exchange, the latest in a 6-year interval series shows:

	%	Distribu	ution of	Shareho?	ldings
		1963	1969	1975	1981
Persons		54.0	47.4	37.5	28.2
Financial institutions of which:		30.3	35.9	48.0	57.9
Insurance Cos Pension Funds Unit Trusts Investment Trusts		10.0 6.4 1.3 11.3	12.2 9.0 2.9 10.1	15.9 16.8 4.1 10.5	20.5 26.7 3.6 6.8
Trabub			10.1	10.)	0.0

The long run trend towards increasing indirect investment through financial institutions can be explained mainly by the growth of occupational pension schemes and the tax advantages they and life offices have been able to offer. The economic climate of the 1970s and 80s may have encouraged saving through deposit accepting institutions, especially building societies linked with home ownership.

- 2. The abolition of the investment income surcharge and of tax relief on life policy premia is likely to discourage saving through insurance-based investments and encourage direct share ownership.
- The Business Expansion Scheme has the effect of encouraging wider share ownership although its primary purpose is to raise capital for unquoted companies. It gives tax relief of up to £40,000 per annum at the top marginal rate available to individuals who subscribe for new equity shares in qualifying unquoted trading companies. Recent figures show that some £44m has been raised by 29 of the 34 funds that have so far been approved under the scheme. The remaining funds plan to raise at least a further £8m. Best estimates suggest that around 80% say £35m would have been invested by 5 April 1984. And to this must be added amounts subscribed on a direct basis not through a fund under the scheme though these are thought to be small.



- 4. In FSC Division's view the main barrier to wider share ownership is educational. There is no difficulty in getting advice from brokers or banks and no ground for the view that share investment is too complex for the ordinary saver. The public's perceptions of risk may be improved by the measures that may be introduced to implement Gower. But the changes afoot in the Stock Exchange are not thought by FSC to have much bearing on wider share ownership. Indeed commissions on small deals could rise after the abolition of the minimum charges; this was a short term response in New York when they abolished minimum commissions though in the longrun the emergence of new 'no frills' brokers may have offset this effect.
- 5. There may be a growing appreciation of the benefits of wider share ownership. But it seems unlikely that there will be any sudden or sharp reversal in the trends set out in paragraph 1 above.



17/5/84.

SHARE OPTIONS

Share options have been tackled by two previous items of legislation - in 1980 and 1982 - and by one, the most important, currently in the Finance Bill. The proposed legislation is aimed particularly at Directors and key employees. Subject to certain limits and conditions, it will remove tax from unrealised gains on the exercise of share options leaving just capital gains tax to be paid at the time of eventual disposal of the shares. This is expected to have the following beneficial effects:

- enable small and growing companies to attract key personnel without the need to pay high salaries;
- give ailing companies the chance to attract new talent looking for rewards in terms of longer term growth;
- help large and established companies retain (Particularly against foreign competition) and motivate highly valued executives;
- give employed individuals a chance of accumulating wealth, perhaps sufficient to enable them to start their own enterprise;
- encourage employee involvement and wider share ownership.

The 1980 legislation is of a different character. It links share options to SAYE savings arrangements and is It is thus aimed at employees within a company generally. principally concerned with motivation and encouraging wider share ownership. Some 292 schemes have been approved. Latest figures - April 1983 - show that shares to the value of around £350m have been granted under the 1980 scheme, and it is reckoned that some 150,000 employees have participated. This legislation complements that of the 1978 profit sharing schemes, the limits of which have been raised by the Government, and which also encourages wider share ownership. Finally, the 1982 legislation introduced a limited relief for non-approved option holders, allowing a spread of 3 years for payment of the tax chargeable on exercise of an option. This period is to be increased to 5 years, but only for schemes involving options granted before 6 April 1984 (later schemes will be expected to take advantage of the arrangements described in paragraph 1 above).

OTI NOTE DH SHARE OF TOOLS



3. The Department has been pressing for some years for an executive-type share option scheme. There was originally some discussion as to whether the rules ought to limit participation to unquoted companies but it was eventually decided that the scheme should be available widely, and Finance Bill proposals largely reflect what the Department asked for. There do, however, remain one or two points of difficulty. For example the rules as currently proposed would exclude from benefit of relief any person who has or would acquire a 'material' interest - more than 5% of the ordinary share capital - in the company. Mr Trippier, in particular, considers this too restrictive for the smaller company and has written to Mr Moore on the subject.



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10 DOWNING STREET

From the Private Secretary

No longer

the caree

18 May 1984

Der David

SEMINAR ON INDUSTRY AND EMPLOYMENT

My letter of 9 May set out the agenda for the 25 May meeting and promised the circulation of a number of papers. I attach a copy of the two papers produced by the Secretary of State for Employment and a copy of the No. 10 Policy Unit note on wider ownership. Attached to the latter are factual annexes prepared by DTI on employee shareholdings in privatisation issues; steps to promote wider share ownership; and share option schemes. The paper on export promotion will be circulated next week.

I would be grateful if you could ensure that these papers are retained within Private Offices. If Ministers wish to seek briefing on them the papers should be shown only to those who need to see them, without reference to the meeting at which the papers are to be discussed.

I am sending copies of this letter to David Normington (Department of Employment), Michael Reidy (Department of Energy), John Ballard (Department of the Environment), Elizabeth Hodkinson (Department of Education and Science), Callum McCarthy (Department of Trade and Industry), Alex Galloway (Chancellor of the Duchy of Lancaster's Office), David Young (Manpower Services Commission) and Richard Hatfield (Cabinet Office).

Your smart

Andrew Turnbull

David Peretz, Esq., H.M. Treasury.

SECRET AND PERSONAL: CMO

FROM: HP EVANS

18 MAY 1984

cc:

CHANCELLOR OF THE EXCHEQUER

Circulation list attached

ACTIVITY AND THE LABOUR MARKET: RECENT DEVELOPMENTS

I attach a note by David Owen which assembles and interprets recent evidence. I draw your attention to the following points:

- (i) There is a small rise in the output estimate of GDP in the first quarter of 1984, despite the effect of the miners' dispute (paragraphs 1-3). Revisions to late 1983 mean that the output estimate is now showing 3 per cent growth on a year earlier for both Q4 1983 and Q1 1984.
- (ii) The last CBI quarterly survey shows a clear contrast between the <u>low</u> level of labour shortages and the <u>average</u> level of plant utilisation in manufacturing (paragraph 13).
- (iii) Our view of employment continues to rely heavily on heroic assumptions about undercounting: in the next month or two we should get some more information from the June 1983 Labour Force Survey.
- 2. We are starting to update the budget forecast and I will shortly be sending you a note on the proposed policy assumptions.

HPE H P EVANS EVAN 1815

NOTE ON ACTIVITY AND THE LABOUR MARKET

SUMMARY

21 May1984

Activity

- *GDP (output measure) rose a little in the first quarter despite some effect from the miners' industrial action. Our best assessment is still that GDP (average measure) has been growing at about 3 per cent per annum (paragraph 1 to 4).
- *The miners' industrial action is estimated to have reduced the index of production by about 2 per cent in March. On this basis the direct effect of the action (ie rejecting only lost coal production) may have reduced industrial production by 3 per cent in April, the first full month of the strike (paragraph 10 to 11).
- *The trend in manufacturing output has been upwards since the last quarter of 1982. By the first quarter of 1984 output was over 3 per cent higher than a year earlier. Further growth seems likely in Q2, in line with the FSBR forecast (paragraph 12).
- *Non oil export volumes rose sharply at the end of last year and maintained the improvement into the first quarter of 1984 (paragraph 9); consumer spending fell back in Q1 but retail sales recovered strongly in April (paragraphs 6 to 7).
- *April CBI survey suggest that capacity utilisation in manufacturing is close to its long run average, but shortages of labour are at historically low levels (paragraph 13).
- *The cyclical indicators suggest that the recovery will continue throughout 1984 and into 1985, as foreseen in the FSBR forecast (paragraph 14). The April CBI Industrial Trends Survey points to continuing increases in demand and output in manufacturing (paragraph 15 to 16).

Labour Market

- *There are currently conflicting indicators in the labour market: total employment grew 200 thousand between March and December, consistent with steady tightening, but unemployment has continued to rise.
- *Unemployment (UK, seasonally adjusted excluding school leavers) fell by 1,000 in April following a small rise in March. When allowance is made for the build up of special measures the underlying trend is still upwards. The stock of notified vacancies appears to have stabilised at about 150,000 (paragraph 21 to 23).

ACTIVITY

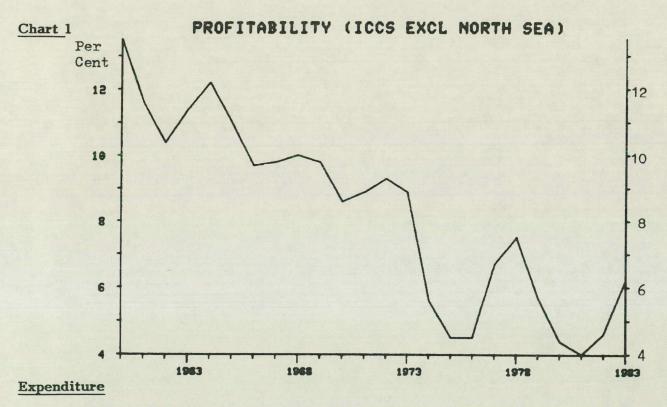
Gross Domestic Product

- 1. Preliminary estimates being published on 21 May show that the <u>output measure of GDP</u> rose a little in the first quarter of 1984. The latest figures include an upward revision to the fourth quarter of 1983 and output growth between the first quarters of 1983 and 1984 is put at almost 3 per cent. Growth over this period was affected adversely by the miners' overtime ban and, more recently, by the strike which began on March 12. The industrial action may have reduced GDP(O) by ½ per cent in the first quarter, with only a negligible effect on the fourth quarter of 1983.
- 2. Complete estimates for the first quarter for the income and expenditure measures of GDP will not be available until next month. Limited information on the components, which has become available since the FSBR forecast was published, suggests that, as expected, the <u>average measure of GDP</u> may have grown rather less rapidly than the output measure between the first quarters of 1983 and 1984. Allowing for the uneven path of the average measure over the past year the latest figures continue to suggest an underlying rate of growth of around 3 per cent per annum.

Table 1: Gross Domestic Product (1980=100) GDP(E) GDP(O) GDP(I) GDP (Average) CSO **FSBR** latest **Forecast** 1982 H1 101.0 98.9 100.7 100.2 100.1 H2 101.8 99.9 101.0 100.9 100.9 1983 104.7 100.7 H1 103.6 103.0 102.9 H2 105.4 102.9 104.7 104.3 103.8 1984 Q1 103.5 Per cent change 1983 on 1982 3.6 2.4 3.3 3.1 2.8 1983 H2 on 1982 H2 3.5 3.0 3.7 3.3 2.9

3. The small rise in the <u>output measure</u> of GDP in the first quarter reflects increases in **some** service industries, although distribution output fell back from the high levels recorded in the second half of 1983. Manufacturing output was fairly flat following strong growth in the second half of last year, while output of the energy sector fell because of the effect of the miners' industrial action.

4. Estimates of the expenditure and income measures of GDP for the fourth quarter of 1983 have been revised upwards slightly since the FSBR was published and both measures now show growth in excess of 3 per cent through the year. A significant feature in the recovery of the income measure has been the sharp rise in industrial and commercial company profits which were almost a quarter higher in 1983 than in 1982. DTI provisionally estimate that non-North Sea ICCs real profitability (net pre tax rate of return) rose from 4.6 per cent in 1982 to 6.2 per cent in 1983, the highest level since the peak of the previous profitability cycle in 1978, when it was 7.5 per cent. Bank of England estimates suggest that profitability may have been as high as 7 per cent in the fourth quarter of 1983.



- 5. The recovery in final domestic expenditure between mid 1982 and the end of 1983 was dominated by growth in personal consumption. Recent data are consistent with the FSBR forecast of a more broadly based growth in expenditure in 1984 with investment, stockbuilding and exports rising sufficiently to offset some slowdown in the growth of consumer demand.
- 6. Preliminary estimates indicate that <u>consumers' expenditure</u> fell by 1 per cent in the first quarter reflecting lower retail sales of most types of goods as well as a reduction in new vehicle registrations. Most of the fall was accounted for by <u>expenditure on durables</u> (particularly vehicles) which fell back by over 7 per cent from the high level of the fourth quarter. This represents the first significant hesitation in

the durables "boom" which began in the first half of 1982 - by the second half of 1983 expenditure had increased by over 30 per cent. The FSBR forecast envisaged a flattening out of durables expenditure during the course of 1984. Non durables' expenditure fell only slightly between the fourth quarter of 1983 and the first quarter of 1984 - lower expenditure on food and clothing and footwear, probably reflecting deferred spring purchases due to the cold weather and late Easter, was almost offset by higher energy consumption.

7. Despite the fall in total consumers' expenditure in the first quarter longer term comparisons confirm the continued though moderating upward trend: expenditure was up over 2 per cent between the first quarters of 1983 and 1984. Over the same period real personal disposable income may have risen by as much 4 per cent, implying a small rise in the saving ratio. This contrasts with the FSBR forecast which looked to a small decline in the saving ratio for 1984 as a whole. However the provisional April retail sales figure points to a strong recovery in expenditure, tending to support the view that the first quarter figures were adversely affected by special factors. Retail sales in April were $3\frac{1}{2}$ per cent higher than the average level in the first quarter and were even higher than the record levels reached in the second half of 1983. On balance therefore the latest information does not cast serious doubt on the FSBR forecast that consumers' expenditure will grow by 3 per cent between 1983 and 1984.

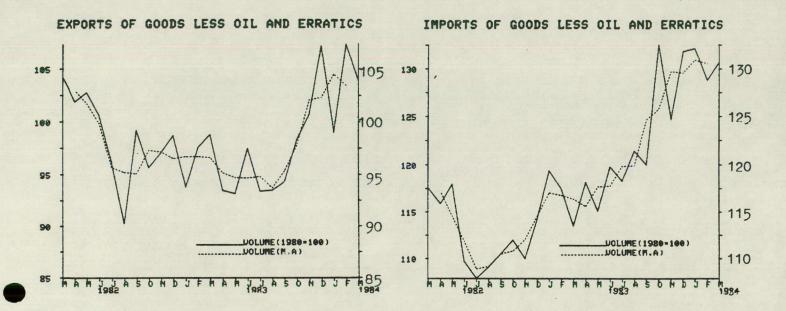
Table 2: Personal Sector Expenditure

(£ billion 1980 prices)

		Saving Ratio (per cent)	Consumers' expenditure	Private investment in_dwellings	Retail Sales Volume 1980=100	Private Housing Starts (Thousands per month)
1982	3	9.4	34.9	0.8	102.9	11.9
	4	9.1	35.6	0.9	104.1	11.8
1983	1	8.5	35.5	1.0	105.5	15.3
	2	8.2	36.1	1.0	107.3	13.6
	3	8.0	36.5	1.0	108.3	13.1
	4	9.0	36.7	1.1	110.4	13.7
1984	1	(10.0)	36.3	n/a	108.5	14.2
1984	Jan				107.7	13.8
	Feb				109.5	14.6
	Mar				108.3	14.2
	Apri	1			112.2	n/a

- 8. Private sector housing activity seems to have remained strong in the first quarter of 1984 following growth of over 20 per cent in private sector investment in dwellings between 1982 and 1983 (part of which reflects increases in expenditure on grant aided improvements). Private housing starts rose by 3½ per cent between the fourth quarter of 1983 and the first quarter of 1984 though they remain below the erratically high figure recorded in the first quarter last year when weather conditions were unusually favourable.
- 9. The most recent figures for <u>non-oil export volumes</u>, of which about 80 per cent are manufactures, have been encouraging: the first quarter figures saw the fourth quarter recovery maintained and some further growth (about 1½ per cent). A similar picture emerges for <u>non-oil import volumes</u>, where the rise seems to have slowed down in recent months after an increase of 8 per cent between the third and fourth quarters of 1983. As a result non-oil exports and import volumes are now both running some 7-8 per cent above their average 1983 level.

Chart 2



Industrial Sector

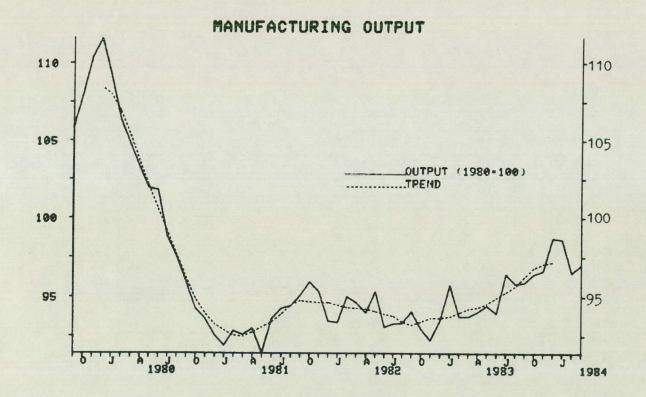
10. The miners' industrial action has so far had two stages: an overtime ban which began on 31 October and a strike which started on 12 March. The overtime ban probably reduced the level of industrial production by about 1 per cent in February. The index of production figures for March (published on 17 May) are the first to be affected by the strike itself, and they suggest that, simply because of the lost coal production, industrial production may have been reduced by just over 2 per cent. On this basis production in April, the first full month of the strike, may turn out to be almost 3 per cent lower as a direct result of the action. The indirect effect on other industries is thought to have been small so far. The most likely impact is on the steel industry. In March steel production in total was quite high but there was a fall in April because of coal shortages at the BSC's Scunthorpe works.

Table 3 Miners' Industrial Action

		Direct impact of action on Index	Index Production	of (1980=100)
		of Production (CSO Estimates)	Published (17 May)	Adjusted for Industrial Action
1983	Oct	-	102.2	102.2
	Nov	0.4	102.5	102.9
	Dec	0.6	104.1	104.7
1984	Jan	0.8	104.5	105.3
	Feb	1.0	102.7	103.7
	Mar	2.2	101.3	103.5
	April (Projection)	2.8	n/a	

11. The effect in April is equivalent to nearly 1 per cent on GDP in total.

Chart 3



- 12. After allowing for the estimated direct effect of the industrial action the trend in industrial production continues to be strongly upwards the strike adjusted index for the first quarter was almost 1 per cent above the level in the fourth quarter and 4½ per cent higher than the same period last year. In addition to strong growth in the output of the energy sector there was a steady upward trend in manufacturing output throughout 1983. Although the CSO provisional estimate for March implies little growth in manufacturing output between the fourth quarter to 1983 and the first quarter of 1984 the April CBI Industrial Trends Survey suggests a more buoyant picture: it recorded the highest balance of firms reporting increased output over the past four months (+25) since January 1977. A further sharp fall in spare capacity was also recorded. Forward indicators suggest that growth in manufacturing output between the first halves of 1983 and 1984 is likely to be close to the 4 per cent forecast in the FSBR.
- 13. Capacity utilisation seems to have increased strongly in recent months, continuing the trend which began in 1981: the proportion of firms reporting that they were working below a satisfactory full rate of operation fell from 65 per cent in the January CBI survey to 59 per cent in April. Despite high levels of unemployment and the large drop in output since 1979 utilisation now appears to be at roughly the average level of the past 20 years, supporting the view that there has been widespread scrapping of inefficient plant since 1979. Only 14 per cent of firms expect the shortage of plant capacity to constrain their output over the next four months but this is also close to the past average. It compares with 80 per cent who cite the shortage of orders or sales as a constraint a level previously associated with cyclical troughs. The proportions of firms reporting skilled labour shortages or problems meeting overseas delivery dates are still at historically low levels.

Chart 4



FORWARD INDICATORS OF ACTIVITY

- 14. The cyclical indicators published on 18 April 1984 continue to suggest that the economy will remain with the upswing phase of the business cycle through 1984 and into 1985. The longer leading indicator which indicates turning points in activity approximately one year ahead hesistated last Autumn but has since resumed its upward path, mainly reflecting rises in share prices and to a lesser extent housing starts. The coincident and shorter leading indicators both rose in January but, based on only partial information, fell back in February.
- 15. The quarterly <u>CBI Industrial Trends Survey</u> for April indicated a further increase in the level of business optimism. The balance of manufacturers reporting increased optimism was +26 compared with +27 in January. However there is normally a seasonal improvement in optimism in April and after allowing for this the balance fell 13 points [NB NOT FOR USE until 14.30 22 May: the seasonally adjusted fall in the CBI optimism balance has not yet been reflected in the published cyclical indicators, but it will have a

downward effect on the longer leading indicator to be published on 22 May. However this will be offset by the buoyancy of share prices, leaving the overall assessment in paragraph 14 unchanged]. Total new orders are reported to have strengthened throughout manufacturing over the past four months and firm's expectations suggest further increases in demand and output over the next four months. While these figures point to a continuation of the upward trend in manufacturing output the balance expecting higher output fell back slightly from the high levels recorded in February and March. This, taken together with the weaker business optimism balance, may point to a slight slowdown in output growth in the months ahead.

Manufacturers' investment intentions for plant and machinery and buildings strengthened slightly between the January and April CBI surveys. On the basis of these responses the CBI now forecast an increase in manufacturing investment (including leasing) of about 7 per cent between 1983 and 1984. This is similar to their forecast published in January and the CBI conclude that the Budget measures have not yet had much effect on firms reported investment intentions. The next DTI survey of investment intentions will be published next month. The DTI survey last December pointed to manufacturing investment growth of 9 per cent in 1984 and the FSBR forecast, which included an allowance for the bringing forward of investment plans in response to the Budget, projected an increase of 14 per cent.

LABOUR MARKET

17. Labour market indicators which have become available since the completion of the FSBR forecast have been broadly in line with previous trends. The picture continues to be rather mixed: Department of Employment provisional estimates suggest that a firm upward trend in employment was established in the second half of 1983 but the underlying level of unemployment – after allowing for the effects of Special Employment Measures – continued to rise throughout 1983 and the first four months of 1984. These figures – which suggest very rapid growth in the working population – appear to be inconsistent with DEm estimates of growth in labour supply of some 200 thousand († per cent) during 1983. The Budget forecast projected continuing growth in employment and a flattening out of unemployment during 1984. By early June the results of the 1983 Labour Force Survey will should provide more reliable data.

18. The supplementary estimate of the employed labour force - which includes an allowance for additional growth in employees and the self employed of 65,000 per

quarter - grew by 200 thousand between March and December following a period of continuous decline since 1979. As has been pointed out recently this growth is almost entirely accounted for by the (inevitably very uncertain) allowance for assumed undercounting in the basic employment series. However, even excluding this allowance, there was a significant increase in estimated employment in the fourth quarter of 1983.

Quarterly change (000s) **Employed** Labour Force **Employees** (incl self in employed) **Employment** 1982 1 -33 -54 -107-1283 -142-166 4 -75 -98 1983 1 -50 -75

Table 4 Whole Economy Employment*

+26

+55

+117

0

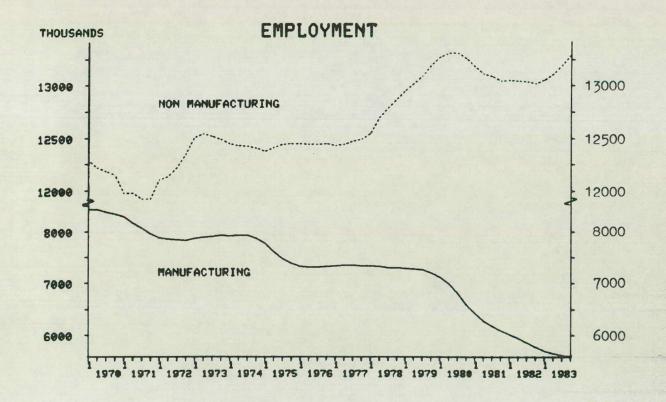
+27

+92

2

34

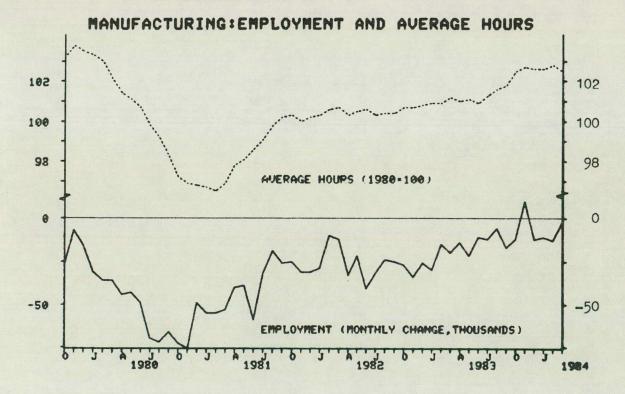
Chart 5



^{*} Including allowance for undercounting.

19. The movements in total employment through 1983 are accounted for by a progressive slowing of the decline in manufacturing employment together with an accelerating upward trend in employment outside the manufacturing sector. By the second half of 1983 the rate of decline in manufacturing employment had fallen to an average of 8000 per month and this rate - somewhat below the trend rate of decline during the 1970s - was maintained in the first quarter of 1984. The April CBI survey points to continued small falls in manufacturing employment in the months ahead.

Chart 6



Average weekly hours worked in manufacturing have now levelled out following the substantial increases during the second half of 1983. During the first quarter of 1984 the index of average hours was 1½ per cent higher than in the first quarter of 1983. This reflects a reduction in hours lost through short time working and an increase of over 15 per cent in overtime hours. Overtime per operative and short time are now at levels similar to those recorded during the cyclical peak in 1979. It may be that for many firms, as confidence in growth strengthens, future increases in the demand for labour (man hours) will be met more by rising employment than by further increases in average hours.

Table 5: Manufacturing Sector: Employment and Hours (GB)

Seasonally adjusted except CBI balance

		Average monthly change (000s)	CBI Expected Employment Balance	Average weekly Hours (1980=100)	Total hours of overtime (millions)	Short-time hours lost (millions)
1982	1 2 3 4	-17 -32 -27 -28	-36 -39 -42	102.6 101.7 100.8	10.2 10.0 9.9	1.8 1.9 1.6
1983	1 2 3 4	-22 -16 -12 -5	-43 -45 -29 -25 -24	100.8 101.0 101.0 101.6 102.6	9.8 9.5 9.7 10.6 11.4	1.7 1.4 1.2 0.8 0.5
1984	1 2	-9 n/a	-16 -12	102.6 n/a	11.1 n/a	0.6 n/a
1984	Jan Feb Mar	-11 -13 -2		102.6 102.8 102.5	11.0 11.3 11.1	0.6 0.6 0.6

The level of UK unemployment (seasonally adjusted, excluding school leavers) fell by 1,000 in April following a modest increase of 8,000 in March. These figures taken together are encouraging when compared with the sharp increases of around 30,000 in both January and February. But the trend is still upwards, though slower than in the first half of 1983: in the six months to April the average rise in the number of claimants was 12,000 per month.

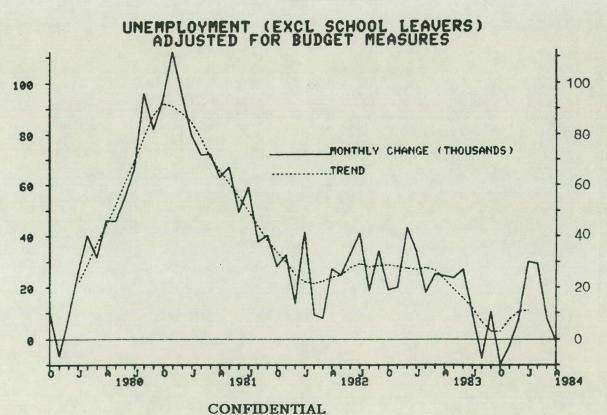
Table 6: Unemployment (excluding school leavers

Average monthly change (Thousands)

		8- (
	Adjusted for Budget Measures	Adjusted for Budget Measures and SEMS
	+31	+34
	+28	+31
	+26	+28
	+25	+31
	+4	+11
	-2	+14
	+22	+24
	+30	+34
y	+29	+30
	+8	+9
	-1	+5
		Adjusted for Budget Measures +31 +28 +26 +25 +4 -2 +22 +30 y +8

22. Changes in adult unemployment in the second half of 1983 were significantly influenced by the expansion of certain special employment measure (SEMS) - notably the Community Programme. When allowance is made for this (see Table 6) the underlying growth in uneployment over the past six months has been faster. Since January the effect of SEMS on the adult count has more or less levelled out and little further increase is anticipated.





23. The trend in the stock of vacancies notified to Job Centres has now levelled out at about 150,000 following fairly strong growth through most of 1983. Vacancies fell back somewhat at the end of 1983 but this was in part accounted for by a reduction in Community Programme vacancies which had boosted the stock in the second and third quarters. The inflow of vacancies increased sharply in April but the average inflow in the last three months, at 193 thousand a month, was unchanged from the previous three months.

Table 7: Notified Vacancies

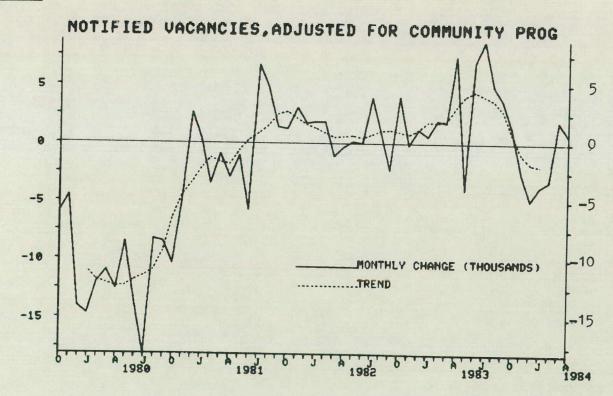
Stock, Thousands

excl
Commun
Program

1982 3 111 109

,	Total	Community Programme
1982 3	111	109
4	115	112
1983 1	124	119
2	135	123
3	160	140
4	161	144
1984 1	147	135
January	148	136
February	145	137
March	147	134
April	148	133

Chart 8



CIRCULATION LIST

CHIEF SECRETARY

FINANCIAL SECRETARY

ECONOMIC SECRETARY

MINISTER OF STATE

SIR PETER MIDDLETON

SIR TERENCE BURNS

MR BAILEY

MR LITTLER

MR MONCK

MR BYATT

MR CASSELL

MR KEMP

MR BATTISHILL

MR EVANS

MR LANKESTER

MR SEDGWICK

MR LAVELLE

MR LOVELL

MR ODLING-SMEE

MR SCHOLAR

MR RIG ALLEN

MR MELLISS

MR BOTTRILL

MR FOLGER

MR CULPIN

MRS LOMAX

MR MOWL

MR PERETZ

MR RILEY

MR WHITE

MISS SINCLAIR

MR KELLY

MISS PEIRSON

MR ROBSON

MR SHIELDS

MR HORTON

MR P D SPENCER

DR P A ROWLATT

MR GLEED

MR OWEN

MR RITCHIE

MR DAVIES

MR POWELL

MR C KELLY

MR HARTLEY

MR NORGROVE

MR A SMITH

MR LORD

MR PORTILLO

MR RIDLEY

UNCLASSIFIED

FROM: M EVERSHED

DATE: 21 May 1984

MR FOLGER

cc Mr Grimstone

ENCOURAGEMENT OF EMPLOYEE, AND WIDER, SHARE OWNERSHIP

I have seen a copy of your note to Mr Peretz of 15 May.

Note 2 on employee share schemes has lost an entry in Annex B en-route through your word processor:

"BP (September 1983) + "

Should be followed by

"Cable and Wireless (December 1983) + "

The actual table entries are identical - which may be the cause of the error.

Mus Bose 215.84 previous papers, asap, please (Mula be on HF/01)

M EVERSHED

POLICIES AFFECTING THE LABOUR MARKET AND EMPLOYMENT

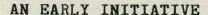
Memorandum by the Secretary of State for Employment

Our strategy for economic success is popularly expected to reduce unemployment. We must hold to that strategy as giving us the only genuine prospects of higher employment. Its pursuit is essential to stimulate the efficient operation of both the product and labour markets. My personal belief is that we stand a good chance of seeing unemployment fall over the next three years to the lower end of the range outlined in my accompanying paper, and of course we shall need by then to see a significant declining trend in the level of unemployment.

- 2 Against this background I believe:
 - (i) we must take an early initiative to win the public argument about increasing jobs, extending enterprise and seeking opportunities for growth wherever they may be found. This requires a concerted campaign, fed both by our achievements so far and by any new moves to remove labour market constraints and encourage enterprise. I and my Ministerial colleagues in the Department of Employment will certainly seek to play a full part in this but clearly the role of other Ministers, particularly the Chancellor and the Secretary of State for Trade and Industry and their colleagues is vital.
 - (ii) in addition, we must consider what steps we might take in line with our main economic strategy in perhaps 18 months from now if we judged further action was necessary.

Why was

SECRET AND PERSONAL



- 3 Inflexible labour practices and loss of management control have made the labour market inefficient and been a significant impediment to the creation of jobs. Since 1979 we have done a great deal to improve the position. Annex 2 lists the action already taken to establish more realistic wages, to provide a more balanced framework of industrial relations law, to improve the quantity and quality of skills, to remove constraints on labour mobility and to promote enterprise through self-employment and encourage greater flexibility in working patterns generally. These measures often take time to show, but the signs are growing eg skill differentials are widening, the pay of young workers is declining relatively to that of adults and restrictive working practices are being removed.
- What more can we do? The first need is not new measures but to make clearer to people the freedom that now exists for them to generate jobs whether for themselves or for others. The Government can and must continue to remove constraints on the operation of the labour market. The creation of employment then depends on the response of those working within it, notably employers. We must ensure that they do know how much we have already done to remove the burdens and constraints on the creation of jobs. And we need to put this in the context of a general shift towards enterprise and a capital owning democracy in which people are encouraged to employ others. This calls for a concerted public campaign conducted by all of us.
- 5 Secondly, I also believe that we can and should do more within our economic strategy:

SECRET AND PERSONAL

SECRET AND PERSONAL

- (a) to remove any further constraints that we can on the labour market to bring supply and demand for labour into better balance; and
- (b) to assist the two groups of people who will continue over the next three years to be especially badly hit by unemployment the young and the long-term unemployed.
- Annex 1 lists a range of possibilities of further action to meet these requirements. We must decide which of these to pursue and who should do them and we need to fit their announcement as each comes forward into the public campaign I have in mind.
- 7 Two of them would serve particularly well to give fresh focus to the message of that campaign:
 - (i) one would be Lord Cockfield's "passport for a job" idea adapted to a voluntary basis (paragraphs A.8-10 of Annex 1). In essence this would enable smaller employers to employ young people at a modest wage, free of tax and NI, and exempt from the Employment Protection Acts. Such a scheme would dramatically remove the administrative burdens from employers and could unlock a whole raft of extra jobs from small employers who are put off by all the paperwork and regulations. If this were to happen it would be a most effective example of the link between deregulation and job creation.

Of course, there are a host of problems, both of policy and operation, that need to be thought through to see whether it really could work and main legislation would be needed. But I hope colleagues will agree that we should really see whether we can overcome the problems and mount some version of the scheme, possibly limited in the first instance to small businesses, where the employment impact is likely to be greatest, and for young people;

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SECRET AND PERSONAL

- (ii) we could also build on the success of the Enterprise Allowance Scheme introduced only last year. This helps unemployed people set up in business on their own account by paying them an allowance of £40 a week for a year in place of benefit. It is not only highly popular, but a first class illustration of our philosophy of encouraging enterprise and self-help in a capital owning democracy. We could continue it on the basis of opening it to all comers instead of rationing applications and we could make it easier for people to qualify (paragraph E.8 of Annex 1).
- 8 There would be a cost to these moves though in the case of the passport scheme it is a loss of revenue rather than public expenditure. While I cannot yet be certain, I believe there is a good chance that I could contain the cost, on the provisional estimates, within existing PES provision, notably from savings from the Youth Training Scheme.
- If we found we could make either or preferably both of these moves, we could use their announcement very effectively within the publicity campaign to get over our message to employers and the public generally on our positive approach to the generation of more jobs through freer operation of the labour market.

FURTHER ACTION

10 Separately from that initiative it must be prudent to consider what we might do if no clear sign of a declining trend in unemployment were to appear by early 1986, recognising that it takes time for any action to have effect.

SECRET AND PERSONAL

- 11 . It is plainly crucial that any such action then should not appear to run counter to our economic strategy and is generally accepted as tackling priority problems. It would also be necessary to select measures which are labour intensive and sure in their employment effect and preferably inclined towards those who are then being most hardly hit. It seems to me that this requires us to turn attention to twoparticular areas of potential action:
 - the extent to which existing special employment programmes can be readily increased and the time lag involved. Possibilities are the Community Programme (in general or for the very long-term unemployed - paragraph C.8-9 of Annex 1) and a temporary resuscitation of the Job Release Scheme by moving the age down again from 64. Both of these schemes could be expanded to have a relatively quick and substantial impact on unemployment
- (ii) the extent to which, with adequate preparation, we could quickly replace those public expenditure programmes and projects which are less labour intensive with these which would raise employment quick?
 - These approaches would have expenditure effects which would have to be considered within the public expenditure programmes generally and in accordance with the economic strategy.

CONCLUSION

13 I invite colleagues' views of the above assessment and suggestions.

SECRET AND PERSONAL

POLICIES AFFECTING THE LABOUR MARKET AND EMPLOYMENT

POSSIBILITIES FOR FURTHER ACTION

- 1. Jobs depend not just on the development of products and services for sale, but on the responsiveness of the labour market to the needs of the product market. Over the years inflexibilities in the labour market external to companies and in their internal labour markets have damaged competitive efficiency, enterprise and job creation. It has accordingly been an important aim of Government policy since 1979 to free the labour market from restrictions and improve its operation in the interests of employment.
- 2. This Annex sets out possibilities for further action (including some already in train or under consideration) to stimulate employment though facilitating the working of the labour market. Annex 2 records relevant action already taken by the Government since 1979. The material in both Annexes is grouped into the following five sections, though each contributes in complementary ways towards the basic objective:

Section A: Labour costs - wage and non-wage

Section B: <u>Labour relations</u> - the legal framework, employee involvement

Section C: Labour quality - vocational education and training

Section D: <u>Labour mobility</u> - placement services, housing and pension policies, regional policy

Section E: Patterns of work - changes in the length of working life and working week, the balance between full-time and part-time work, self employment.

SECTION A: LABOUR COSTS

A.1 The links between pay, unit labour costs and jobs, in both private and public employment, are now much more widely recognised and understood. Levels of pay and conditions of employment have to take account of all the various claims on the employer's resources. Not only must they enable employers to recruit and retain employees, reward effort and skill and promote productivity: they will significantly affect current competitiveness and profitability and therefore the course of investment which will influence future employment.

A.2 It is necessary to produce conditions in which pay reflects these realities. This can be done by explanation, aided by example-setting in the public sector; by removing statutory or contractual limits on the setting of wages in relation to the employer's circumstances; by removing and discouraging arrangements which depend on comparability; by introducing and stimulating flexibility in payments reflecting skill and experience; and by removing or minimising fiscal and statutory burdens on employers which discourage employment.

A.3 Action already taken to bring about these changes and induce greater flexibility in pay determination is set out in Annex 2. There are several options for further action to deal both with wages and with non-wage costs or employment conditions.

(i) Wage issues

(a) Central Government employees

A.4 For the negotiated groups of government employees the scope for giving further weight to market factors is limited. First, as the level of pay settlements has fallen, the room for manoeuvre on differentials, whether for skill, age or location, has become much smaller. Secondly, the unions have been consistently opposed to widening skill differentials, and this resistance can be expected to increase. For the non-negotiated groups, progress depends

on the extent to which the Review Bodies are willing to give greater weight to market factors than they have in the past; and, where they do not, on the Government's willingness to take the politically difficult step of altering the Review Bodies' recommendations.

(b) Removal of Government constraints

A.5 Ministers have decided not to abolish Agricultural Wages Boards but will shortly be re-considering the future of <u>Wages Councils</u>, although the obligation to observe ILO Conventions prevents any radical change before 1986. The Attorney-General has advised that current ILO obligations preclude not only complete abolition, but also the exclusion of substantial categories such as young people, part-time workers or small firms. E Committee have previously considered a number of less radical options - such as imposing new statutory duties on the Councils - but so far have concluded that none would be effective or worthwhile.

(c) Lowering the relative pay of the young

- A.6 The Young Workers Scheme could be developed to have a greater effect. One possibility would be to extend the scheme to young people beyond age 17 eg to under 20 year olds, among whom the level of unemployment is particularly high. With the level of subsidy remaining at £15 a week for up to 12 months, provisional estimates indicate that extending the scheme to young people under 20 at the current earnings limit levels (£50 a week) might mean an additional take up of up to 60,000 in 1985/86 (take up for 17 year olds for that year is estimated at about 50,000). Additional gross public expenditure would be some £13 million (current PES provision for YWS in 1985/86 is £45 million). If the scheme were limited to employees of small firms (say under 10 employees) this should improve its cost effectiveness, but would reduce the increase in take up and net additional jobs.
- A.7 It would perhaps be more sensible as an alternative to maintaining current earnings limits to have an age related wage criterion (eg less than £50 per week for those under 17, less than £60 for those under 18, less than

£70 for those under 19). This would have a number of effects: it would retain the relative depressing effect on wages and increase take up, but might also have a counterbalancing detrimental effect on employment opportunities for adults.

A.8 A more radical option would be to restyle or replace the Young Workers Scheme with a new scheme along the lines of Lord Cockfield's suggested "Passport for a Job". Under such a scheme employers would be free to offer, and young people under age 18 would be free to refuse or accept, jobs offering a cash wage of up to say £45 a week without any obligation on either party to pay income tax or national insurance and outwith the scope of all (or most) statutory employment protections. While many of these conditions may already apply to young people (for example NI, contributions are only payable above a wage level of £34, and in practice few young people fall within scope of many employment protection provisions), the object would be to encourage more employers to take on young workers by removing all such obligations.

A.9 The inducement to the employer would lie in the removal or reduction of the burden of paper work entailed in taking on any new employee (for example, by removing the requirement to conform to PAYE procedures even though the employee's wages are below the tax threshold). Young people would benefit from improved job prospects no PAYE and NI contribution (provided contributory benefit cover was maintained by granting NI credit). From the Government's point of view there would be a revenue loss but no public expenditure commitment. NI contribution exemption for employers and employees could cost fl5 million a year and 'tax lost' could be around £21 million a year. Deadweight (ie those who would have been employed even within the exemptions) could be considerable; if experience resembled the Young Workers Scheme, deadweight might be as high as 80 per cent.

A.10 The Scheme could of course be extended beyond 16 and 17 year olds to under 20 year olds. This would increase the revenue loss and possibly the complexity of the scheme as it moves into the area of adult wage rates. If on

the other hand the scheme were limited to small employers, deadweight and revenue losses could both be less.

A.ll Such a scheme would need main legislation. Though simple in concept, considerable policy and operational problems would have to be resolved before it could be confirmed feasible eg on tax and national insurance (where exemption from tax and NI contributions would break the principle that earnings create a liability), movement in and out of the scheme (possibly creating a wage trap), and the implications for the Youth Training Scheme. Preliminary exploration of the practicalities is in hand.

(d) The effect of the tax and benefit systems

A.12 The impact of PAYE on casual and part-time employment is worth examining. If the level at which PAYE impacts on such employment could be raised or casual workers given limited exemptions from its operation, there could be advantage in removing some of this activity from the black economy and in promoting more such employment. There will be problems of definition; some cost from exempting existing jobs in the "white economy"; and opportunities for people to take several part-time jobs and avoid tax on them all.

- A.13 The <u>interrelationships between the tax and benefit systems</u> have been intensively scrutinised; in particular, in 1982 the CPRS made a number of recommendations to overcome the detrimental effects on employment. These are worth re-examining and could be placed on the agenda of the Central Unit's work for the DHSS reviews of social security. They include:-
 - (i) overcoming effects on the <u>wage floor</u> by uprating supplementary benefit in line with the <u>lower</u> of increases in prices or earnings; and finding new way of subsidising low income families that would be more effective than FIS and less expensive than increasing child benefit or tax thresholds.

- (ii) reducing the <u>lack of incentive to take up work</u> by changing benefit rules to require acceptance of <u>any</u> job that paid no less than benefit; or reintroducing a 'wage stop' on benefit.
- (iii) encouraging take up of <u>part-time work</u> by allowing more earnings to be retained without equivalent benefit loss.

Making a major inroad into the poverty and unemployment traps will, however, be extremely costly and, as the recent Green Paper showed, will depend crucially on maintaining firm control of public expenditure over a number of years.

(ii) Non-wage issues and employment conditions

A.14 Turning to non-wage issues and employment conditions, one option to be considered is to repeal the statutory protections against unfair dismissal and other lesser protections (eg action short of dismissal). This would be to return to the pre-1971 position although statutory protections would need to be retained for such dismissals as those from closed shops or for union membership, on the grounds of sex or race and, under an EC Directive, for employees the ownership of whose undertaking is transferred.

A.15 Repeal apart, a thorough review of the statutory provisions undertaken this year has identified the following main options:

- (a) extend the qualifying period to 2 years for all employments (reducing the number of complaints by about 25%) or to 3 years (reducing complaints by about 43%);
- (b) exclude all very small employments (a cut-off at 5 employees would remove about 1.4 million employees from scope; a cut-off at 10 employees about 3 million);
- (c) exclude "new" businesses on a variety of possible formulations;

- (d) a voluntary option of arbitration where the employer and the claimant agree to accept the outcome as an alternative to a settlement by a tribunal, subject to a statutory ceiling on the amount of compensation which could be awarded;
- (e) make arbitration compulsory for "minor" cases, say complaints made in the first 1 to 2 years following qualification.
- A.16 The review also identified a number of administrative and other possible improvements to the industrial tribunal system, mainly as an alternative to more radical action, on which work is already in hand:-
 - (a) increasing the efficiency and cost-effectiveness of tribunals;
 - (b) ending the requirement on tribunals to provide detailed written decisions in all cases;
 - (c) exploring the possible benefits of revising the Code of Practice on Disciplinary Practices and Procedures in Employment;
 - (d) discouraging the growing use of solicitors at the conciliation stage;
 - (e) more tentatively, exploring ways of reducing the number of appeals to the Employment Appeal Tribunal.

SECTION B: LABOUR RELATIONS

Bl. A more balanced framework of industrial relations law assists realism in collective bargaining and facilitates the management of change and the pursuit of efficiency. At the same time labour relations and efficiency within companies can be improved through action by employers to involve employees more closely in decisions that affect them at their place of work. Better operation of the labour market requires action on both aspects of labour relations.

INDUSTRIAL RELATIONS LEGISLATIVE FRAMEWORK

- B2. The action already taken is set out in Annex 2. Possibilities for further action under consideration are:
 - (a) The ways in which the maintenance of essential services can be better assured through primary legislation;
 - (b) Alternative proposals have been developed which would enable employers to lay-off without pay employees whose work was affected to any extent by industrial action. The first would relieve employers of their contractual and statutory obligations when a major dispute in a key industry had widespread effect. The second approach would provide the same reliefs if selective action was taken by only some employees of the same employer.
 - (c) The possibility of deeming all substantive and procedure agreements legally enforceable (or attaching trade union immunity to their observance), if employer opinion generally came to be supportive of such steps, if it was possible to be confident that employers would use the remedies the law would provide, and if negotiated agreements were improved to the point that they would bear the weight of legal interpretation.

EMPLOYEE INVOLVEMENT

- B3. Action already taken is reported in Annex 2 (paragraph B3). The prime requirement is to allow practice to develop according to the needs and circumstances of the individual enterprise and to avoid imposition of a rigid and predetermined approach from outside. We shall therefore continue our twin aims of resisting the draft 'Vredeling' and Fifth Directives of the EC while supporting and encouraging good practice, mainly through Ministerial speeches.
- B4. Employer organisations are also active. In the last year the Industrial Participation Association and the Institute of Personnel Management have issued an authoritative Code of Practice and together with the CBI are holding this year numerous involvement seminars and conferences up and down the country. It will be open to us to review the position at some future date in the light of company reports under Section 1 of the 1982 Employment Act.

SECTION C: LABOUR QUALITY

- C.1 For the labour market to work properly those within it must have the right skills and/or the capacity to attain them. Over the years those emerging from our education system have too often been less broadly educated than their counterparts abroad; too little attention and status has been given to technical education and to education of the least able young people. Within the electronics industry shortages of certain skills are already appearing, leading to the risk of sharp upward pay movement. More generally, the low number of technicians and craftsmen, the low percentage of managers with formal qualifications and of workers with any vocational qualifications at all, together with the restrictive practices surrounding the apprenticeship system, have all contributed to a relatively poor economic performance.
- C.2 Details of action already taken to improve the relevance of education and training to industrial and commercial requirements are in Annex 2. Further possibilities are:

(a) Educational initiatives

- C.3 The <u>action programme within the schools sector</u> will, if successful, lead to a series of connected initiatives over the next few years. In collaboration with other Government Departments it will be aimed as far as possible at those points within the decentralised education system which have a direct influence on the curriculum and examinations. In particular:
 - (i) Initial teacher training will be reformed to improve the selection of trainees and to make training courses academically more rigorous, more closely related to the practical work of teaching in the schools and taking more account of pupils' employment opportunities in industry and commerce.
 - (ii) As the objectives of the 5-16 curriculum and for each main subject in it come to be defined, local education authorities will be

asked to report on how the curriculum in their schools measures up to the defined objectives and to take steps to secure that it does.

- (iii) The objectives for the school curriculum will emphasise practical skills and applications for pupils of all ages and ability levels, building on and complementing what the Technical and Vocational Education Initiative (TVEI) is doing for a selection of 14-18 year olds.
- (iv) Among the objectives for the school curriculum is the introduction of pupils to the nature and origins of our society, including the economic facts of life.
- (v) The 16+ examinations will be changed so that grades are awarded only if candidates have demonstrated required levels of understanding and competence - broadly defined, rather than mainly an ability to recall facts in an orderly fashion.
- (vi) All school leavers will be offered a record of their achievements at school, including success in activities other than examinations which throw light on their personal qualities.
- (vii) The proposed legislation to give parents elected by their fellow parents control of most school governing bodies with important responsibilities for the affairs of the school will enable parents to contribute to the objective, which they regard as crucial, of better preparing pupils for jobs.
- C.4 If this ambitious action programme for school education were to be extended, one further change worth examining to improve the quality of the labour force would be greatly to broaden the sixth-form studies of every student, by replacing the A level examinations with an examination more on the lines of the German Abitur. This would require all those aspiring to post-16 qualifications and higher education to continue to study to age 18 a much

wider range of subjects than is now common, including mathematics and science, thus strengthening the technological base of the labour force as well as its competence in other areas.

- C.5 In Higher and Further Education the need is probably less for radical innovations, but for more and better of what we now have. In this situation a number of possibilities exist which are already receiving attention.
 - (i) Developing comprehensive part-time education and training provision for the 16-18 age group, by extension of the Youth Training Scheme or otherwise.
 - (ii) The further development of activity like the DES Professional,
 Industrial and Commercial Updating Programme.
 - (iii) Extension of the Information Technology in Higher Education initiative.
 - (iv) Substantially increased output of graduates in the technologies.
 - (v) The potential of distance learning for delivering education economically.

(b) Training loans

C.6 The 1984 White Paper "Training for Jobs" stated that the Government would "examine, in collaboration with the Manpower Services Commission and others, the possibility of establishing a loan scheme for adult trainees". DE are conducting a preliminary study of the need for and practicability of a loan scheme. The study will be submitted to Ministers soon with a view, if they agree to proceed, to designing a pilot scheme and issuing a consultative document in mid-July. Action thereafter will depend on the response and on whether main legislation is required for the type of scheme favoured.



(c) Training the long-term unemployed

C.7 As was also stated in the 1984 White Paper, the Government are considering an MSC proposal for more training or work preparation in the Community Programme with the object of making those on it more employable. The proposal is that funds should be made available for up to 13 weeks off-the-job training or work preparation - though the average would probably be about 6 weeks - for up to 50,000 of the 130,000 places on the Programme. Participation by employers and individuals would be voluntary and no training allowances would be paid in addition to the remuneration under the Programme. Officials are examining the proposal and will shortly put a recommendation to Ministers.

(d) The very long term unemployed

- C.8 The possibility is being examined of a scheme of community work for all very long-term unemployed with the dual object of maintaining their employability and enabling them to contribute to the satisfaction of local community needs. Alternatives might be to offer this type of work permanently or to permit those who have already completed a placement under the Community Programme to be eligible for another one after a further period (perhaps six months) of unemployment. People could continue to become re-eligible in this way for as long as necessary. To some extent this latter option is already possible under the current procedures, but if eligibility conditions were eased the client group would be enlarged.
- C.9 At present 656,000 people have been unemployed for 2 years, of whom 300,000 have been unemployed for up to 3 years and 191,000 for up to 4 years, so the numbers such a scheme would need to cover are very large. Experience with the Community Programme indicates that finding enough sponsors and suitable projects to meet such a demand would be a problem. The costs would also be very substantial; using Community Programme criteria every 10,000 places would cost annually £43 million gross £18 million net.

SECTION D: LABOUR MOBILITY

- D.1 Artificial constraints on mobility, both between jobs and from one place to another to take up employment, hinder the proper working of the labour market. Government measures can of course only permit and encourage mobility and not enforce it. In any case, geographical mobility involving a change of residence is likely to have only a marginal impact on unemployment when labour markets are depressed throughout the country. Mobility policies can thus be seen as complementary to regional policy which aims to contribute to a better geographical spread of employment.
- D.2 There is already a fair degree of mobility. The Government has taken steps to encourage this (see Annex 2) and further possibilities are set out below.

(a) Housing

- D.3 The Government has already undertaken to introduce measures to abolish solicitors' conveyancing monopoly and is reviewing the house purchase process generally, through the work of the conveyancing Committee and the official group, to see whether it can be simplified and speeded up. Of greater potential significance is the legislation to be taken in 1985/86 for the decontrol of rents for new lettings. Other possibilities include:-
 - (a) further development of accessible low cost home ownership, especially through shared ownership schemes;
 - (b) the direct provision of homes by building societies for sale, rent or shared ownership if, as proposed, the societies are given powers to hold land;
 - (c) issuing a new circular (now in draft) which will advise authorities to increase the availability of land for housing, including the maximum use of inner urban land, and make its provision more in tune with market demand;

- (d) taking more positive steps, eg the use of powers of direction, to encourage the disposal of sites on the land registers for development or new use;
- (e) speeding planning applications by improving efficiency and further streamlining the system-revision of the General Development Order and extending the Enterprise Zone concept more generally as Simplified Planning Zones;
- (f) reducing the disincentive effect of Capital Gains Tax on resident landlords;
- (g) amending the rules relating to resale of ex-council houses to free purchasers of the requirement to repay discount after 3 years instead of 5 as at present.

(b) MSC Mobility Schemes

D.4 The cost effectiveness of these schemes — employment transfer and job search — is currently under review and proposals will be put to Ministers in the early summer. The possibility exists for a further extension of these schemes to encourage more people to move home or to search for jobs outside their own area. At present under 5000 people use the job search scheme each year. This number could be increased by extending eligibility for the scheme, for example by removing the requirement on employers to show that a job could not be filled by local labour. Proposals are being considered by the MSC for an extensive reorganisation of the network of Jobcentres which should provide a more extensive but more cost effective placement service.

(c) Pension Schemes

D.5 The 1983 Manifesto included a commitment to ease the position of the "early leaver" under pension schemes. The Government proposals for legislation requiring pension schemes to revalue early leaver's pension rights by 5% per annum up to pension age have been published in a consultative

document, and the new legislation is planned for next Session. The Inquiry into Provision for Retirement being conducted by the Secretary of State for Social Services is also examining ways of encouraging personal portable pensions, one of the aims being to open up fresh avenues for making pension rights even more portable from one job to another.

(d) Regional Policy

D.6 The new scheme of regional assistance — to be implemented this Autumn — aims to be more cost—effective, to be more job—related and to provide greater parity of treatment between manufacturing and service sectors. It will provide for the payment of Regional Development Grant at the higher cost of either a fixed amount for each new job created in the Assisted Areas by eligible projects or a fixed percentage of approved capital expenditure, subject to a cost per job ceiling. Levels of grant have yet to be fixed but there is a case for relatively high job grants consistent with the policy aims of cost—effectiveness and sound investment. The job grant element element will have to take account of the EC policy of controlling State aids (which we support) but it might be worth reconsidering the current EC ceiling of about £3000 per job, in the interests of maximising the employment impact of the new scheme.

SECTION E: PATTERNS OF WORK

- E.1 Greater responsiveness in the labour market implies improvements in the supply of labour through adaptation to new working patterns as well as adjustments in labour costs and the acquisition of new skills. Responsibility for using labour more flexibly and adaptably must lie primarily with employers. Many British firms are indeed developing schemes for new work patterns including flexible working time, more part time working and different forms of employment contract including homeworking. The scope for this varies with the nature of the business and the composition of the workforce.
- E.2 There is considerable current interest in worksharing as a means of reducing unemployment. Though this has advantages in theory in allowing highly flexible working time, there are severe practical limitations. Furthermore, work sharing has to be accompanied by pay-sharing if it is not to make business uncompetitive and push up the rate of inflation. It will be difficult to reach and enforce agreement on this.
- E.3 In the light of this, Government intervention should be directed to breaking down barriers whether of institutions, working practices or habits of thought to the adoption of worksharing where it does have economic advantages. Any positive measures of this kind would go beyond the current more limited objective, which is to use worksharing (eg through early retirement and short and part-time working) as special employment measures. These have represented a trade-off in the short term between Government objectives because, although their initial impact on unemployment can be quite rapid, some of them may as a result tend to relieve downward pressures on wages, so producing an adverse price effect in the longer-term.
- E.4 The attractiveness of worksharing in the longer term depends upon the view taken of the way in which the economy will develop. In the light of current uncertainties, it would be wrong for the Government to advocate or recommend irreversible moves towards sharing out work which might damage competitiveness and hinder employment prospects, especially with the prospect

of a declining labour supply in the 1990s. A draft EC Recommendation on Working Time is to be considered by the June 1984 Council of Ministers, but it is important to maintain Government opposition to draft EC Directives in this area (eg on part-time work) which would have a restrictive effective on flexible working.

- E.5 These considerations do not apply to policies for encouraging the trend towards increasing self-employment as a more prominent pattern of work. (DE estimates are that the number of self-employed rose by over 350 thousand between mid 1971 and December 1983).
- E.6 Action already taken by the Government to encourage new working patterns is described in Annex 2 and further possibilities are set out below.

(a) Small Firms

E.7 The DTI are reviewing both the possibility of simplifying the present schemes of support for small firms and of making further efforts to remove administrative and statutory burdens; most further action also now rests with other Departments. The DTI are also reviewing the future of the Small Firms Loan Guarantee Scheme (see para El of Annex 2) which ends this month. A further possibility would be careful scrutiny of the tax and NI systems to ensure no discrimination against the self-employed, though NI contributions for the self-employed have already been held below the level properly due.

(b) Enterprise Allowance Scheme

E.8 This scheme for helping unemployed people set up in business is also being currently reviewed. An increase in the rate at which people enter the scheme over the next 3 months was announced on 1 May and this will contain the current waiting lists. If the scheme was made available on a demand-led basis to all who qualify, the take-up could rise annually to an estimated 70,000 at a cost of around £68 million. If the qualifying period of unemployment was also reduced from the present 13 weeks to 8 weeks, the number could rise to around 80,000 at an annual cost of £78 million.

(c) Effect on enterprise of insolvency law reform

E.9 The proposals contained in the White Paper on insolvency law reform will serve to reinforce public confidence in business standards. Some proposals are designed to increase pressure on company directors and managers to keep a close watch on the financial position of their companies so that difficulties are recognised at an early stage and also to prevent abuse of limited liability by those who deliberately drive their companies into insolvency only to start up again. There is concern that the tougher regime of disqualification and the imposition of personal liability will have an adverse effect on risk-taking especially on venture capital concerns involved in a number of new high risk companies. These should be looked at again to ensure that the right balance between encouraging enterprise and protecting the public has been struck.

(d) Part-time working

E.10 The encouragement of part-time working through the Job Splitting Scheme and part-time JRS is under review, including possible modifications to increase their attractiveness. While the low take-up of JSS makes abolition a possibility, it might also be the case that JSS would be greatly enlarged if new jobs qualified. An experiment might be valuable to see whether the extra deadweight involved would be more than offset by the genuine additional jobs created (thereby saving Exchequer money). The Civil Service could also be widely used to demonstrate the advantages of job-splitting: DE is currently working up proposals of its own and other Departments could follow suit.

(e) Limiting overtime

E.11 Discouragement of systematic overtime working as a means of creating employment is often suggested. As a matter solely of arithmetic, if the 11 million hours of overtime currently worked weekly in manufacturing could be transformed into normal hour jobs, it would yield 280,000 more vacancies for the unemployed, though this would of course be to ignore the practicalities of the real world. Moreover, the amount of overtime worked is not, on average,

large: average overtime worked in 1983 by men was about 3 hours in an average total working week of $41\frac{1}{2}$ hours (compared with about 44 hours in 1973). It is often the most efficient and cost effective way of coping with fluctuations in workload or small but regular amounts of work outside normal working hours.

E.12 To limit overtime by law would therefore require exemptions to be made (and administered) for its use where commercially justified. The limitation could in any event be effective in creating employment only if there were no significant increase in employers' costs as a result; and only the employer can determine the comparative costs of overtime as against recruitment. A prime requirement before considering Government intervention seems to be to establish why companies operate with so much overtime as business expands or are they incorrectly appraising the economics of the situation? The evidence is being reviewed, as is the possibility of linking overtime reduction to the Job Splitting Scheme so as to encourage employers who use regular overtime to consider creating two part time jobs as an alternative.

POLICIES AFFECTING THE LABOUR MARKET AND EMPLOYMENT ACTION TAKEN SINCE 1979

SECTION A: LABOUR COSTS

- Al. Action has been taken so far in a variety of ways:
 - Public sector employment. Central government has just under 2 (a) million employees, with a total paybill of nearly £20 billions. For the collectively-bargained groups (over 1 million) the Government's general negotiating stance has been based on the principles that employers should pay no more than is required to recruit and retain at various grade and skill levels; and that affordability (in this context, the need to contain public expenditure) should play a key role. For the groups covered by Review Bodies, the same principles are taken into account both in the government's evidence to, and decisions on the implementation of, the Review Bodies' awards. But the Review Bodies generally give great weight to comparability, and thus follow, not lead, developments in the market. Since 1980, the general level of pay for collectively-bargained groups in central settlements government has been below that for the rest of the economy, while pay increases for the Review Body groups have generally kept pace with or been somewhat ahead of those outside.
 - (b) <u>Wage comparability</u>. Schedule 11 of the Employment Protection Act 1975 (which could be used by unions to require employers to pay wages afforded in other employments) has been repealed and the Fair Wages Resolution rescinded.
 - (c) Fiscal action has been taken to lower the cost of employing labour. The abolition of the National Insurance Surcharge,

ANNEX 2.

combined with the planned restructuring of First Year Capital Allowances, will substantially reduce the present tax bias in favour of investment and against employment. The abolition of investment income surcharge and the lightening of Capital Transfer Tax will help potential employers to assemble or retain capital. Increases in the income tax threshold in the last two budgets will help to induce people to seek work more actively, though this will be a long haul.

- (d) The Government has also sought to keep down labour costs by protecting employers from NI contribution increases. In 1979, the standard (not contracted-out) NI contribution rate was 6.5% of relevant earnings for employees, and 13.5% (including 3.5% NI surcharge) for employers. From October 1984, the rates will be 9% for employees, and 10.45% for employers (there being no NI surcharge from that date). In other words, employers will have been released entirely from the earlier 3.5% NI surcharge, and the increases needed in the national insurance contribution (excluding the NIS) have been imposed mainly on employees (to the extent of 2.5%), while employers have been shielded so far as possible by increasing their contribution by only .45% over the same period.
- (e) Statutory burdens on employers associated with employment have been relaxed. In 1979 the qualifying period of employment for the protections against unfair dismissal was increased from 26 weeks to one year. The Employment Act 1980, among other relaxations, further increased the qualifying period to 2 years for employment with employers employing 20 or fewer employees; and in the unfair dismissal procedures, both qualified the test of "fairness" (so that the size and administrative resources of smaller employers were taken into account) and shifted the onus of proof away from the employer.
- (f) More realistic wages for young people have been encouraged. This has been done directly through the Young Workers Scheme, which now

provides for employers to claim weekly payments of £15 for up to 12 months for each eligible young person (mainly 17 year olds) employed at less than £50 a week. The £25 a week limit on reimbursement to employers of allowances paid under the Youth Training Scheme has similar effects.

A2. It is not possible to disentangle the effects of the Government measures from the impact of economic influences generally on pay determination within industry and commerce. There is, however, still a continued stickiness in the way in which employers adjust wages to their particular circumstances, evidenced in the way that wage increases have, despite recession, remained higher than price inflation. But there is evidence that skill differentials have widened, that the pay of young workers declined sharply relative to that of adults between 1982 and 1983, and that in some sectors apprentice pay has been reduced under new training agreements.

SECTION B: LABOUR RELATIONS

INDUSTRIAL RELATIONS LEGISLATIVE FRAMEWORK

- Bl. Trade unions have lost immunity for inducing, etc industrial action outside restricted definitions of what is lawful (eg for secondary picketing, secondary action, disputes not between an employer and his employees wholly or mainly concerned with terms and conditions of employment). They are now at risk to injunctions (with the sanction of unlimited fines if they are not observed) and damages (subject to limit). Requirements in commercial contracts about union membership or recognition have been voided and industrial action to enforce them no longer has immunity. Dismissals from closed shops are unfair unless they have been overwhelmingly approved in secret ballots. Dismissal of strikers at only one establishment of an employer is no longer unfair.
- B2. When enacted, the Trade Union Bill will ensure that all voting members of union executives are elected by secret ballots; that trade unions will have no immunity for industrial action if a secret ballot of the members concerned is not held; and that union political funds need to be approved by a secret ballot every 10 years.

EMPLOYEE INVOLVEMENT

B3. The Government believes that managers can secure better results, including better technical standards and the acceptance of necessary change, where they voluntarily consult workers about decisions affecting them. Steady progress is being made. For example, the last authoritative survey showed a 6% increase in the previous 3 years in the number of establishments with joint consultative committees — to 37% in all establishments and 76% in establishments with over 1,000 employees. Section 1 of the 1982 Employment Act provides that firms with more than 250 employees should state in their Annual Reports the specific steps they have taken to further employee involvement. This provision is now in operation and we shall be examining the first results later in the year.

SECTION C: LABOUR QUALITY

C.1 Since 1979 sustained attention has been given to the ways in which education and training can support employment. A more coherent policy framework has been established and action taken both to improve education as a preparation for working life and to relate training for particular jobs much more closely to the requirements of industry and commerce.

The Contribution of Schools

- C.2 The Government's policy to raise standards in schools includes the objective of equipping pupils throughout the ability range with a broad range of skills, competence and understanding. This will improve their preparation for training and employment. It is part of the aim that the school curriculum should be broad and balanced, relevant to the world of work with an appropriate emphasis on practical applications, and differentiated in accordance with ability and aptitude. As this action programme takes effect over time, school leavers will enter the labour market better grounded in personal qualities, attitudes and skills for training and employment.
- C.3 In 1981 the Secretaries of State for Education and Wales set out the policy objective in broad guidance to the education service and asked LEAs to prepare curricular policies for their areas accordingly and to report on these in due course: reports have since been required by 30 April 1984. In January 1984 the Secretary of State for Education and Science announced the longer-term aim of raising the attainment of 80-90% of pupils at age 16 to the level now expected and achieved by the average pupil over a range of subjects and skills; this aim is to be achieved by a more closely defined curriculum (which would extend to the promotion of personal qualities and attitudes as well as subject learning), improved methods of assessment, including the 16+ examinations, and enhanced teaching quality.

Training and Vocational Education Developments

- C.4 The 1981 White Paper "A New Training Initiative: A Programme for Action" set out three national objectives for the reform of skill training, for the vocational education and training of the young and for adult training. A specific action programme was set towards the NTI objectives of which the main features were introduction of the new Youth Training Scheme; the establishment of "Open Tech" to improve access to training and re-training opportunities; a target date of 1985 for training to recognised standards in place of time-serving and age restricted apprenticeships; greater vocational relevance in the school curriculum; and an examination of the sharing of training costs as between trainees, employers and the tax payer. Since the White Paper the Industrial Training Board system has also been substantially reformed.
- C.5 The January 1984 White Paper "Training for Jobs" describes something of what has been achieved so far and the further action already under way or planned. The principal features are:
 - (a) The <u>education service</u> has been encouraged to improve the preparation which it offers young people for work through
 - developments in the school curriculum
 - the introduction of the Certificate of Pre-Vocational Education
 - the introduction of the Technical and Vocational Education
 Initiative
 - strengthening schools' and colleges' links with employers (the Colleges-Employers Links Projects Programme is especially relevant);

- (b) the roles and responsibilities of employers, trainees and Government have been clarified on the basis that training is an investment which needs to be attractive financially. Restrictions on access to training and the deployment of trainees must be removed. The main responsibility for training rests with employers, but trainees can contribute by accepting realistic allowances and Government by helping with the transition from school to work, training the unemployed and funding experimental courses in new technologies and techniques.
- the Youth Training Scheme has been successfully launched and 1984-85 will be a year of consolidation with an emphasis on improving the quality of training. It fully meets the UK's obligation under the EC Resolution on Vocational Training of July 1983, to ensure that (within 5 years) all minimum age school leavers should receive training or work experience. (The UK currently expects to receive about £200 millions towards the cost of YTS and related programmes from the European Social Fund for 1983/84. Recent revision of the Fund rules will enable us to claim even more in future.)
- (d) some industries have made substantial progress towards reforming their arrangements for training in occupational skills (including apprenticeships) though much still remains to be done to meet the 1985 target. The wider, longer-term, aim is to adopt a coherent system of training standards and certificates of competence, covering achievement in vocational education and training, both initially and throughout working life.
- (e) the MSC is initiating a national campaign to raise awareness of the need to offer more opportunities for adults to acquire, improve or update their skills, and, with DES, is encouraging closer local collaboration between employers and education and training organisations. MSC's adult training programmes will be restructured to help many more people with job-related training,

as well as training geared to the needs of the unemployed. Skillcentre training has been put on a commercial basis by setting up the Skillcentre Training Agency, and Open Tech will be extended;

- (f) public sector provision for training and vocational education is intended to be made more responsive to employment needs by increasing MSC's resources for purchasing work-related non-advanced further education in England and Wales to about one quarter of the total provision in this area.
- C.6 Further initiatives have also been taken in the education sector.
 - The DTI's Industry/Education Unit is working in collaboration with industry and commerce, for example to provide industrially relevant resource material for schools, colleges and Examination Boards; to encourage industry-related expertise in both initial and in-service teacher training; and to introduce new technology into all schools eg through the various "micros" schemes;
 - opportunities for adults are being enhanced through the DES Professional, Industrial and Commercial Updating Programme, which is now in its stride;
 - DES's Information Technology in Higher Education Initiative is substantially increasing the output of IT-qualified graduates and diploma-holders;
 - the Further Education Unit has been strengthened;
 - the planning exercise of the National Advisory Body for Local Authority Higher Education, related to intakes in autumn 1984 and after, substantially increases the proportion and total effort within Advanced Further Education devoted to work-related courses (especially engineering and business studies);

- first degree engineering courses in universities and polytechnics have been much evolved in the light of the recommendations of the Finniston Committee (1979) and subsequent attention to this topic;
- the MSC has collaborated with the DTI in the development of Information Technology Centres (ITECs) of which 150 have been approved.

The use of skills

C.7 A more competitive industry also requires the full use of trained people's skills. This is the responsibility of industry and commerce itself and there is evidence of progress. Large companies, such as Pilkingtons, ICI and Michelin have been making agreements to provide for greater interchange of process workers and craftsmen at the workplace and for more "hybrid" multiskilled workers. In some cases, eg BSC, British Shipbuilders and provincial newspapers, market forces have provided the main spur to breaking down old demarcations. The introduction of new technology has encouraged the same developments, eg at BL, Rolls Royce and Blue Circle. Such changes owe much to the application of greater management confidence and resolve and the involvement of employees affected.

SECTION D: LABOUR MOBILITY

D.1 Since 1979:

- (a) changes in housing policy have helped to free the housing market and therefore allow greater mobility. Home ownership has been a start has been made on reducing restrictions on private letting; the rate of stamp duty on house purchase has recently been reduced; and in the public sector the National Mobility Scheme and the Tenants Exchange Scheme have served to make it easier for Council tenants to move from one area to another. No reliable assessment can be made of the impact of these measures on willingness to move: from the 1971 to the 1981 Censuses there was a fall in total mobility probably due in part to the reduced employment opportunities in recent years; in 1982-83 the National Mobility Scheme accounted for over 4500 moves at national (as distinct from County) level, the Tenants Exchange Scheme for up to 4000 moves. The latter will be reinforced by a Statutory Right to Exchange for public sector tenants contained in the Housing and Building Control Bill which should shortly receive Royal Assent;
- (b) the Government has taken a number of steps to speed up the performance of the planning system. Duplication between planning authorities has been reduced. Approved structure plans now cover the whole of England apart from Avon, and a large number of local plans are in preparation. The proportion of planning applications decided within 8 weeks has risen from around 60% in 1979 to around 70% in 1982 and the first three quarters of 1983. A range of measures to speed up the handling of planning appeals has also been carried forward and the average decision time for all appeals was 21 weeks in 1983 compared with 29 weeks in 1979. A range of new initiatives has been developed to assist inner city areas: land registers, urban development grant and the establishment of

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urban development corporations in London and Liverpool. All these measures are now leading to increased private sector housing activity in urban areas;

- (c) the MSC's placement services have been improved. The computerised vacancy circulation system has been implemented nationwide. Arrangements have been made for Jobcentres and private employment agencies to display details of each other's services in order to encourage jobseekers to make full use of both private and public sector assistance in finding employment. The Professional and Executive Register (PER) has been given a separate trading account and required to cover its costs on this basis. By removing the "social subvention", PER has been exposed to competition from private employment agencies on fairer terms. The MSC Employment Transfer and Job Search Schemes have been extended to cover a wide range of skilled jobs. These schemes help fill jobs where employers cannot find suitable workers locally, by providing grants to unemployed people to move home and take such jobs or to look for work in other areas;
- (d) loss of <u>pension rights</u> can deter people from changing jobs and the Government has encouraged the pensions industry to take action to deal with the problem. Regulations have also been amended to ease the rules for transferring pension rights from one contracted out scheme to another.
- D.2 The December 1983 White Paper on Regional Industrial Development proposes policy changes to contribute to a better geographical spread of employment. It states the Government's belief that the case for continuing with regional industrial policy is now principally a social one with the aim of reducing, on a stable long term basis, regional imbalances in employment opportunities. Regional industrial policy has another justification as the mechanism through which we obtain our share of the European Regional Development Fund: £170m was received in 1983.

SECTION E: PATTERNS OF WORK

- E.1 <u>Small firms</u> often have advantages in achieving the flexible working practices necessary for their survival and growth. Ninety-five per cent of all enterprises in manufacturing employ fewer than 100 people and the small companies' share of manufacturing output has begun to increase in recent years. The Government has done much to assist the establishment and growth of small firms through measures designed to offset their inherent disadvantages, notably in regard to managerial and other specialist resources and the supply of capital. Fiscal measures (e.g. lower Corporation Tax, better stock option arrangements to attract good management) are part of this. The Loan Guarantee Scheme is estimated to have contributed 33,500 net new jobs. The Business Expansion Scheme has also been successful in tapping new sources of equity capital for small firms.
- E.2 The Enterprise Allowance Scheme, introduced as a special employment measure last year, has proved extremely popular among unemployed people as a means of helping them set themselves up in self-employment. It pays them an allowance of £40 a week for up to a year in place of benefit. Some 31,000 people have benefitted from the scheme since it began. The Scheme is cash—limited and applications far outrun places.
- E.3 The Government has also encouraged greater flexibility in working life through more flexible rules relating to retirement. All men over 60 on supplementary benefit can now qualify for the higher long-term rate of that benefit; and unemployed men over 60 get NI credits for future pension and benefit purposes without having to register as unemployed. The Job Release Scheme is now a long standing special employment measure which has encouraged older people (at different points in the 60s for men and at age 59 for women) to retire early and vacate their job for a younger unemployed person. The scope of the scheme for men (other than disabled) has been brought back this year from age 62 to age 64 so it will have a more limited effect.

E.4 Some encouragement has been given by the Government to the spread of part time working through the introduction last year of the Job Splitting Scheme and part-time Job Release as special employment measures. The former scheme makes a grant over 12 months to an employer who splits a full time job into two and recruits one of the part timers from the unemployed: the part time JRS is available to men from age 62 and offers half the full time JRS allowance to those who wish partly to retire and where the part of the job thus released is occupied by someone unemployed. Both schemes are in line with expressed interest in flexible retirement and worksharing but both have had a very low take up so far.

EMPLOYMENT PROSPECTS

Note by the Secretary of State for Employment

- Cabinet on 1 March decided that it would be useful to look in more depth at future employment prospects and the scope for Government action to improve them.
- This note is concerned with future employment prospects. Attached to it is a background paper prepared by my officials, in consultation with Treasury officials, which examines recent trends of employment and unemployment and their view of prospects for the future.
- The broad thrust of the paper is that, barring unexpected shocks in the domestic or international economies, adult unemployment in three years' time might be expected to fall somewhere in the range 21-31 million.
- I believe that our economic strategy is working and that unemployment will be in the lower part of the range. But the paper points out that the recovery in output has been going on for three years without any effect on unemployment, and also that even within a "shock free" scenario quite a number of things have to go right if we are to see a strong and sustained reduction in unemployment

- At the moment, it is not impossible that unemployment will drift slowly up during this year. Real wages are rising; labour supply is increasing; and the high level of productivity increase most welcome in itself is running ahead of the increase in output.
- If the assumptions in the paper turn out to be pessimistic (eg if there were faster growth in the world economy), we might do better than is suggested. But I think it is prudent also to consider what would happen if there were adverse shocks to the economy, such as a slowdown in the US or world economy or a rise in inflationary pressures. Unemployment might then continue on an upward path into the higher part of the range or could even be above it. And, of course, such an outcome would simply increase the time it took for our economic strategy to pay off in terms of employment and unemployment, and probably damage its credibility in the country.
- The Annex also points out that, if unemployment were to continue at a high level or were to rise further, this would mean disproportionately serious problems for long-term unemployment, for the 18-25 age group, and for particular localities.
- 8 While I am optimistic on the economic and employment front, I think it is prudent to consider the range of possibilities which lie ahead. Given the long-time lags between policy initiatives and their effects, we should consider what we might do and when if things do not turn out as well as I expect.

BACKGROUND PAPER

LABOUR MARKET TRENDS AND PROSPECTS

The UK economy is about to enter the fourth year of recovery from a recession which reached its trough at around the second quarter of 1981. The inflation rate has been halved, output is now growing at three per cent a year, and there has been an improvment in cost competitiveness. Despite these developments, there is no sign of a downward trend in unemployment. To explain this paradox, this paper looks first at the broad trends of development over the past three years and then at more recent trends. It then attempts to draw out the implication for the prospects over the next three years.

THE PAST THREE YEARS

Over the past 3 years, GDP has grown at an average rate of $2\frac{1}{2}$ per cent a year (or 2 per cent a year if North Sea oil output is excluded). But in the early part of this period and before, the rapid growth in real earnings together with high interest rates and a high exchange rate put companies under severe financial pressure. They responded by reducing their stocks and to some extent by resisting continued rapid earnings growth; but they also shed labour, thereby increasing productivity to an unusual extent. In manufacturing, output per person grew at an average rate of over $6\frac{1}{2}$ per cent a year - the fastest sustained growth in productivity since the war - and for the economy as a whole (excluding North Sea oil) it grew by about 3 per cent a year.

- Productivity thus rose to an unexpected degree and, especially in manufacturing, substantially exceeded the growth in output; this had its counterpart in a rapid fall in employment. Over the three-year period, productivity growth, for the whole economy excluding North Sea oil, exceeded output growth by a margin averaging 1 per cent a year, corresponding to the same percentage fall in employment. The average annual fall in employment over the last three years has been about 320,000 in GB manufacturing and about 300,000 for the employed labour force as a whole.
- Demographic growth added significantly to the problem but its effect was partly offset by a fall in the proportion of the population seeking work. Activity rates among prime-age males do not appear to have fallen in response to the recession, but among men of 55 and over there has been a continuing sharp fall which is thought to have been influenced also by the Job Release Scheme and by the increased availability of occupational pensions schemes. Recessionary influences appear, however, to have been mainly responsible for the cessation of the hitherto upward trend in female activity rates in the late 1970s and for their noticeable decline since 1981.
- 5 To summarise: the picture over the last three years, from December 1980 to December 1983, is:
 - (a) an annual average <u>increase</u> in the labour force of about 150,000

- (b) an annual average decrease in the employed labour force of about 300,000
- (c) an annual average <u>increase</u> in unemployment of about 330,000.

THE PAST YEAR

- Unemployment in April 1984 stands at some 800,000 above its level of three years previously, but virtually all of this increase occurred in the two years to April 1983. It is thus evident that, within the three-year averages referred to above, a new trend has been emerging in the course of the past year. Because of the delay in getting statistics there has to be a large element of guess work as to what has really been happening in the past year. We believe it is as follows.
- GDP growth has accelerated in the course of the past year, at 3 per cent for the whole economy or $2\frac{1}{2}$ per cent excluding North Sea oil, some $\frac{1}{2}$ per cent above the three-year average. This has reflected growing consumer and business confidence following reductions in inflation and interest rates, improved prospects for world trade, and a recovery of cost competitiveness. There has been a marked easing of the financial pressures on the company sector and many firms have been rebuilding their stocks.
- In the labour market, the past year has seen a renewed growth in real earnings, accounted for by the fact that, although the growth rate in nominal earnings had fallen to less than half of that of early 1981, the fall in the inflation rate was substantially greater. Productivity continued to rise, and overall competitiveness increased throughout 1983.

Compared with the three-year averages referred to above, the gap between productivity growth and output growth was reversed in the past year with output growth exceeding productivity growth for the economy as a whole by perhaps ½ per cent, corresponding to about 100,000 people in more jobs. The fact that unemployment did not fall appears to be accounted for by an increase in the labour force of over 150,000, but offset by the substantial increase which has occurred in the impact of special employment measures.

PROSPECTS FOR THE NEXT THREE YEARS

The Department of Employment's projections suggest that over the next three years the labour force may be expected to grow at an average rate of about 120,000 a year, with a population effect of about 100,000 a year and an expected increase in activity rates comprising a resumption in the growth of female activity rates, partially offset by a continuing decline in activity rates among older men. These projections suggest that an average increase in employment of 120,000 a year would be just sufficient to maintain unemployment at its present level over the next three years. allowance has also to be made for a probable small decline in the impact of employment measures so that the employment increase required might be put in round figures at 130,000 (or about 0.6 per cent) a year. On these assumptions, unemployment would therefore remain at present levels if output growth exceeded productivity growth by a margin of 0.6 per cent.

- 11 The latest version of the Medium Term Financial Strategy assumes that the average rate of growth of output over the next three years will be slightly in excess of $2\frac{1}{2}$ per cent a year excluding North Sea oil. If productivity were to grow at between $1\frac{3}{4}$ and 2 per cent, which is the rough average of current assumptions, on this basis, there would be no significant rise or fall in the level of unemployment over the next three years.
- But both assumptions could well turn out to be wrong. If the gap between output and productivity growth were larger, employment would grow more rapidly, and vice versa. Different trends in activity rates from those assumed could also produce different outcomes for unemployment. Each percentage point increase by which output growth exceeds productivity growth would lead to an increase in employment of about 200,000 a year and a reduction in unemployment of perhaps 150,000 a year.

Whay

A slower growth of earnings relative to productivity is one of the most important routes through which a more favourable outcome could come about. In time it could lead to increased output relative to productivity, through better competitiveness and profitability and lower interest rates. If annual earnings growth were some 2 percentage points lower, the initial reduction in unemployment on account of increased output alone might be about 50,000 a year in the first few years.

Slower earnings growth would also tend to lead to a slower substitution of capital for labour and the growth of the more labour-intensive sectors of the economy as relative costs and prices in those sectors fell. Such substitution and structural effects would show up at the aggregate level as a lower rate of productivity growth, and hence a reduction in unemployment. But they take time to build up, and the improvement in employment may not be large in the first few years.

15 Faster output growth for reasons other than slower earnings growth would also tend to improve unemployment, unless it was associated with productivity growth that was higher to the same extent. Over the next few years it is possible that output may grow more rapidly, perhaps because of better world economic conditions, an improvement in non-price competitiveness, or an increase in domestic demand. This is unlikely to be matched by an equal increase in productvity growth.

16 On the other hand, the outcome could be less favourable than assumed. The recovery has been under way for almost three years, which by the standards of most post-war recoveries is a long time, without a major effect on employment or any effect on unemployment. This partly reflects the fact that the recession was deeper than on earlier occasions. But this does not necessarily mean that a cyclical downturn will not occur within the next few years, particularly if economic developments abroad lead to less output growth than is being assumed.

The outcome could also be less favourable even if output grows at the assumed rates. It is possible that labour shedding will continue at a fairly high level, and that productivity will grow rapidly as a result, without a correspondingly high rate of output growth. There is still plenty of scope for reducing overmanning before the levels of other major industrial countries are reached. In general, however, faster productivity growth, especially when it is not the result of a labour shake-out, will be accompanied by faster output growth rather than by slower growth in employment.

Departures from the projected labour force trend could also influence the outcome. Although the demographic trends used in the projection are well established, some uncertainty surrounds the projected activity rates. For older males it is assumed that, in view of the retirement bulge commencing in 1985, pressure for early retirement will ease, so that activity rates will decline at a slower rate than in the late 1970s. If they had been assumed to decline at the same rate, then the projected growth in the labour force would have been lower by some 50,000 a year. The projected female activity rates are sensitive to assumptions concerning fertility. If instead of the OPCS central projections their high-fertility variant had been used, the projected labour force growth would again have been lower by about 50,000 a year.

THE PLAUSIBLE RANGE OF OUTCOMES

19 It is evident that substantial uncertainties surround the central assumption of a stable path of unemployment. By

varying a number of key assumptions it would be possible to construct an alternative scenario in which unemployment falls by, say, 300,000 a year. But to do so would involve an exceptionally favourable combination of circumstances. Though unemployment during the recovery from 1932 did fall by over 300,000 per annum for a sustained period, and though the current US job generation shows what economic dynamism can do, there is no precedent in British post-war history for a sustained fall of this magnitude over a three year period. The most rapid rate of fall was at 215,000 a year during the "Barber-boom" of 1972/3, but this was sustained for only 21 months. It would be equally possible, moreover, to construct a pessimistic scenario in which unemployment continues to rise at a rapid rate.

On the above analysis, assuming no major shocks to the economy, it is reasonable to see a band of outcomes ranging from decline in adult unemployment of about 200,000 per annum over the next three years, to an increase in adult unemployment of the same order. On this basis, adult unemployment might be expected to fall in the range $2\frac{1}{2}-3\frac{1}{2}$ million.

THE INCIDENCE OF UNEMPLOYMENT

The bulk of the employment growth over the next three years is expected to occur in the private service sector, with probably offsetting falls in manufacturing and public sector employment. This suggests that female employment is likely to grow more rapidly than male employment. On the

other hand, female activity rates are expected to rise and male activity rates to decline. On balance this suggests a continuation of the recently-established tendency for female unemployment (which at present stands at 9 per cent) to rise somewhat relative to male unemployment (now at 15 per cent). The decline in the relative pay of young people observable over the past few years may contribute to this trend by displacing female employment.

- There is likely to be some change in the age distribution of unemployment. While unemployment rates in the 25-54 age bracket seem likely to remain in the region of 10½ to 11 per cent, unemployment among under 18s (now 23 per cent) is likely to show a marked decline for demographic reasons, because of lower relative pay, and because of the impact of the YTS and YWS schemes. Among 18 and 19 year olds there may be a slight rise from the present rate of 27% as a result of displacement by younger people, and this might also be the case for 20-24 year olds, where the rate is currently 21%.
- Long-term (over 12 months) unemployment is expected to stabilise at not much above its present level of 1.2 million or 37% of all unemployed. The proportion of the unemployed who are long-term unemployed rises consistently with age, to over 45 per cent in the over 55 age bracket. It remains significant for younger people, however, at over 25 per cent for 18-19 year olds.

The regional distribution of unemployment is expected to show no major change, with the possibility of a continuing deterioration in the West Midlands and some improvement in Scotland and the South West. Even on the more optimistic scenario, unemployment will remain very high in some parts of regions and some localities, eg inner city areas.