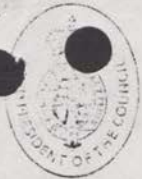


Exec Pd



PRIVY COUNCIL OFFICE  
WHITEHALL, LONDON SW1A 2AT

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Prime Minister

(This was J Vercher's

draft)

MUS 3/12

The attached note on Pay Bargaining  
is circulated on the authority of the  
Lord President of the Council for the  
guidance of all Ministers.

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3 December 1981

## GUIDANCE FOR MINISTERS

### The Effect of the 2 December Announcements on Pay Bargaining

#### Background

The Chancellor's statement on public expenditure, and the associated announcements of the Industry Act Forecast, the Government Actuary's Report, and the Government's decisions on the RSG, make it even more apparent than it has been hitherto that if those in work settle for pay increases in low single figures they will suffer a significant fall in living standards. It is likely that the announcements will lead to a desire on the part of pay bargainers to recoup such losses, and it is therefore particularly important that colleagues take every opportunity to explain why the measures the Government is now taking are right; and why continued pay restraint is necessary, even if it means falling living standards in the short term.

#### The Announcements

The bad news for pay bargainers is:

- (i) Take home pay will be lower because of the rise in National Insurance Contributions.
- (ii) The cost of living (November 81 - November 82 RPI) is now officially forecast to rise by 10 per cent this pay round. This covers the cost increases implied by other announcements (such as higher rents and rates) but of course the sudden rise in those items will have a greater effect on pay expectations than the steady rise in prices throughout the year.
- (iii) Average Earnings are now officially forecast to rise by 7½ per cent in the course of the pay round. Employees in the public services will regard the difference between that and their 4 per cent cash limit as an indication of the extent to which they are being asked to settle for less than the going rate because of their greater job security.

/The good news



The good news for pay bargainers is:

- (i) The worst off are protected from the sharpest rises in costs - many of those paying rents, rates and health service charges receive special assistance in the form of rebates or exemptions.
- (ii) Tight control of public spending means that taxes and/or interest rates are lower than they otherwise would be.

Points to make

1. The long term nature of any successful effort to get the economy competitive again. The Government has always said it would take years, not months. That is why it published a medium term strategy, covering the life time of this Parliament. We mustn't give up now just because things are looking difficult. The difficulties reflect the extent to which we allowed ourselves to fall behind our competitors in the 1960s and 1970s.
2. The Titanic struggle that any administration faces to keep public spending under control. All recent British Governments have faced regular public expenditure "crises". The fact is that public spending rises of its own accord unless it is strictly controlled. Controlling it in a recession is particularly difficult and some rise is inevitable. The Government has done well to keep it to a level which is consistent with a level of public borrowing for next year broadly in line with the projections published in the last budget.
3. We always said those in work would have to have a cut in their living standards. That is a necessary condition of becoming competitive again. It is widely recognised that there was a substantial moderation in pay settlements in the last pay round: but the rise in average earnings still almost kept pace with the rise in the cost of living. Getting competitive again does mean that sooner or later real pay has to be cut: the time for that is now.



4. So the 23 million who are employed will have to make some sacrifice to help the 3 million who are not. The unemployed have to be supported; and they also have to be given the hope of new jobs, which can only come if the employed help create a thriving economy. If wage earners won't accept the sacrifice in their pay packets, sooner or later the sacrifice will be made for them - in more job losses, or in higher taxation, or in higher interest rates.

5. We're starting to get the economy right again: don't let's throw it all away now. Over the five years to 1980, our labour costs (per unit of manufacturing output) nearly doubled. They rose by only one half in Canada, one third in the US, one sixth in Germany and not at all in Japan. But now for the first time for many years our unit labour costs are rising more slowly than those of our competitors. And as the Chancellor said in his statement, output next year is expected to rise by about one per cent, with manufacturing output growing more rapidly. There's a long way still to go, but we're going to get there.