

Prime Minister

A firm rebuttal

of Mr Jenkins's

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proposals.  
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SECRETARY OF STATE FOR INDUSTRY

## THE OUTLOOK FOR INDUSTRY

Thank you for your letter of 13 July. This minute sets out my initial reactions; I hope that we can meet soon to talk in more detail about the prospects for the company sector.

2. I agree, and my paper for Cabinet (C(82)27) indeed points out, that the recovery has shown some hesitation in recent months - though, as you say, the May figures are a little more encouraging. Certainly, as you suggest, there has been some worsening in the outlook for exports, but total order books have been holding up and in some areas (e.g. construction) strengthening. Productivity, and, recently competitiveness, have improved and there has been a strong investment performance by industry. Contrary to what you say the prospect for growth in 1983 has not changed materially since the forecast published at Budget time; and most forward indicators, and outside commentators, also look for a real though quite possibly uneven rise in output over the next year. I fully agree that we must do all we can to encourage this.

3. You suggest an autumn package of measures and announcements. There will in any case have to be autumn announcements, broadly on the same lines as last year or maybe slightly fuller, covering outline public expenditure plans for 1983-84 and our decisions, even if at that stage they are for "no change", in respect of National Insurance Surcharge and National Insurance Contribution rates to take effect from April 1983. In the autumn, too, we shall have, and shall be publishing, the half-yearly economic forecast required under the Industry Act. Measures of the kind



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you propose - or something of the same kind - do indeed come up for consideration then: it would be premature to consider them in detail now.

4. Nevertheless perhaps I can make some general comments.

5. First, I think that we shall have some announcements to make before the Recess - for example, we are in touch about new Enterprise Zones, and you have seen my letter to Arthur Cockfield about Hire Purchase controls.

6. So far as measures which will involve public expenditure are concerned these must I think be considered in the context of the current PESC round. In my view, the international outlook - not least for interest rates - requires us to stick to the public expenditure plans published only four months ago. The reasons are set out in my paper and that of the Chief Secretary; they include the need to keep room for tax reductions which so many people would like to see - including yourself in the case of the NIS. If it were felt that the sort of spending measures you propose should be given priority - and I understand the case for them - I think it is reasonable that this should be in the context of an overall unchanged public expenditure total, and that room for them should be found by savings elsewhere, not necessarily from the provision for your Department.

7. On NIS, the way we, quite deliberately, set about this year's reduction does indeed mean that unless a decision to the contrary is taken in the autumn the current going rate of 2 per cent will revert to 2½ per cent. I appreciate the desirability of not letting this happen, and I note what you say about the desirability of bringing the rate down further. The difficulty we shall face in the autumn, I fear, is that we shall then have to assess the risk that if we do announce a going rate of 2 per cent (or less) from next April, we might find, come the Budget, that we had over-relaxed and that tax increases in other areas were necessary. These other areas would inevitably involve, if not entirely



comprise, individuals. Our record on personal tax, and in the "Why Work" and poverty and unemployment trap areas, is not good and I would be reluctant further to worsen it - particularly in the next Budget. So we shall need to be cautious in the autumn. But I do see the problem involved in reverting to 2½ per cent NIS rate.

8. At the time of the last Budget, as you know, we envisaged for 1983-84 a positive "fiscal adjustment" of around £½ billion, and our current forecast does not alter this materially. The risk is that if we were to go for the sort of package you had in mind we would have to raise taxes or interest rates - and would certainly forego the prospect of making reductions. The difficulties with taxes are obvious. And interest rates, you point out, are one of industry's most important costs; we can only have a reasonable chance of making further reductions if we maintain external and domestic confidence in our financial management. I remain of the view that continued downward pressure on interest rates should be a top policy priority.

9. Final decisions in these matters cannot and need not be taken now. They will have to be reviewed in the autumn and finally settled at the time of the next Budget. Of course I shall bear in mind the merits of the sort of proposals which you put forward. But we all have to bear in mind the risks to recovery that could be involved in misjudged letting up. What we see happening in many overseas countries shows the dangers of succumbing to the temptation of excessive borrowing. The recovery is indeed slow and patchy, but action which prejudiced our general policy stance would be an inappropriate reaction to the slow pace, which is largely caused by events abroad.

10. To summarise, therefore, the points you make, both general and specific, can be taken into account in the autumn. The proposals which involve public expenditure do not necessarily conflict with the need to keep within the present planning totals:



I am sure they will be taken up in the further discussions which the Chief Secretary will be having before final decisions are made. I note what you say about the desirability of a reduction in the National Insurance Surcharge. I accept that there is a balance to be struck between sticking with our fiscal and monetary policies, on the one hand, and on the other the more visible, though not necessarily more real, benefits that might come from measures which require them to be modified. But in my present judgement - which takes full account of the Sam Brittan piece to which you refer - we have currently got the balance about right, in relation to our own circumstances and the world in which we live.

11. In the last Budget we managed to achieve a reconciliation of continued stability in our monetary and fiscal policies - which has led to pronounced progress recently on both inflation and interest rates - with some real and visible tax reductions and other measures which largely benefited industry. I would hope, though of course I cannot promise, that we could achieve the same again for the next Budget; though of course if this were possible it would be a nice question of political and economic judgement how any tax reductions which were available should be shared in the first place between industry and individuals. As I did before the last Budget, I would expect to discuss this with my colleagues before the next one.

*L. N.*

14 July 1982

I am copying this minute to the Prime Minister and other Members of the Cabinet, to the Chief Whip and to Sir Robert Armstrong.