CABINET

CONCLUSIONS of a Meeting of the Cabinet held at 10 Downing Street on TUESDAY 13 NOVEMBER 1973 at 10.30 am

PRESENT

The Rt Hon Edward Heath MP Prime Minister

The Rt Hon Lord Hailsham of St Marylebone Lord Chancellor

The Rt Hon Lord Carrington Secretary of State for Defence

The Rt Hon James Prior MP Lord President of the Council

The Rt Hon Geoffrey Rippon QC MP Secretary of State for the Environment

The Rt Hon Gordon Campbell MP Secretary of State for Scotland

The Rt Hon John Davies MP Chancellor of the Duchy of Lancaster

The Rt Hon Maurice Macmillan MP Secretary of State for Employment

The Rt Hon Lord Windlesham Lord Privy Seal

The Rt Hon Anthony Barber MP Chancellor of the Exchequer

The Rt Hon Robert Carr MP Secretary of State for the Home Department

The Rt Hon Sir Keith Joseph MP Secretary of State for Social Services

The Rt Hon Margaret Thatcher MP Secretary of State for Education and Science

The Rt Hon Peter Walker MP Secretary of State for Trade and Industry

The Rt Hon Peter Thomas QC MP Secretary of State for Wales

The Rt Hon Sir Geoffrey Howe QC MP Minister for Trade and Consumer Affairs

SECRET
THE FOLLOWING WERE ALSO PRESENT

Mr Tern Boardman MP
Minister for Industry (Item 2)

The Rt Hon Francis Pym MP
Parliamentary Secretary, Treasury

SECRETARIAT

Sir John Hunt
Mr J A Hamilton
Mr J A Anson (Item 1)
Mr I T Lawman (Item 2)

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1. The Cabinet considered the economic situation in the light of the October trade figures. Their discussion and the conclusions reached are recorded separately.

2. THE SECRETARY OF STATE FOR TRADE AND INDUSTRY said that there had not yet been time for the overtime ban by the coal miners to have any significant effect, but the National Coal Board (NCB) expected that the loss of production would very quickly reach 20 per cent and would probably amount to 40 per cent towards the end of the following week. The steps taken by Ministers before the weekend had resulted in a favourable presentation of the Government's position in all the national Press, and every opportunity was being taken also to secure further publicity on the radio and television. The NCB were launching a major publicity campaign, in co-ordination with the Government, and were instructing pit managers to seek to persuade the men of the fairness of the Board's pay offer. It was, however, clear that militant elements were seeking an escalation of the dispute directed against the Government's pay policy generally rather than the offer made by the NCB. These elements believed that, if the dispute were extended and a ballot deferred as long as possible, the chances of obtaining a majority for strike action would be enhanced.

THE LORD PRESIDENT OF THE COUNCIL said that, taking account also of the situations in the electricity and oil industries, there appeared to be two main courses of action open to the Government. The first was forthwith to seek a State of Emergency, which would provide the Government with the powers needed to deal with the anticipated fuel crisis, except the power to control fuel prices. There was a Privy Council later that morning and the Emergency Regulations could be laid that afternoon and come into force at midnight. Orders could then be made to restrict the use of electricity for floodlighting, display lighting and commercial space heating and subsequently the oil companies could be given directions on the allocation of oil supplies. The second alternative would be to secure the quick passage through Parliament of the Fuel and Electricity (Control) Bill. The Bill contained powers enabling the Government to impose restrictions on the consumption of electricity, but the powers were not so wide as under the Emergency Regulations. It would be possible to begin petrol rationing under the Emergency Regulations, but since the Emergency Powers would have to be
renewed every month it would be desirable subsequently to pass the Bill. If the oil companies were told to allocate supplies, petrol rationing would become necessary, and it was for consideration whether petrol coupons should now be issued to the public.  In any event all Departments and other public sector bodies should take immediate steps to conserve fuel and a further appeal to the public to conserve fuel was desirable.

In discussion, there was general agreement that the economic and industrial situation warranted immediate action by the Government both to conserve fuel supplies and to reassure public opinion. Whilst there were arguments for delaying action until it was possible to see more clearly the effects of the miners' overtime ban, there was public pressure for early action and the immediate declaration of a State of Emergency might convince the miners that the Government would remain firm in the face of industrial action. The NCB would welcome any step which helped to conserve coal stocks. If however emergency powers were to be taken it would be desirable to resolve quickly - but within the terms of the Pay Code - the dispute involving the Electrical Power Engineers Association (EPEA) since while the EPEA ban on standby duties was in force it was not possible to introduce the rota system of electricity cuts. If the power engineers would not control the cuts the restrictions would have to be of a much cruder nature, leading to widespread and indiscriminate disruption of supplies.

On the other hand it was argued that, although there were increasing signs of shortages of oil, and Esso had been instructed by their parent company to introduce an allocation scheme that week, it would be prudent to clarify the oil supply situation further before deciding to introduce either rationing of motor fuel or an industrial allocation scheme for fuel oil. Although petrol rationing would require a minimum of between 3 and 4 weeks to introduce, no other country had yet adopted it, and the effect upon the Arab oil producing countries of doing so would need to be taken into account. The Government would, moreover, be liable to severe criticism if they announced that a rationing scheme would be introduced without being able to say at the same time when this would be done, the size of the ration and other details.

THE PRIME MINISTER, summing up the discussion, said that the Cabinet agreed that the proclamation of a State of Emergency should be sought that day with a view to conserving fuel stocks and to protect industry, in particular exports. The Secretary of State for Trade and Industry should on the following day make
orders to restrict display lighting and floodlighting and the space heating of commercial premises. Guidance on fuel economy should be issued forthwith to Government Departments and all public sector bodies and the Secretary of State should consider making an appeal for public co-operation in the conservation of fuel during his speech during the debate under Standing Order 9 that afternoon. The Secretary of State for Employment should inform the Confederation of British Industry (CBI) and the Trades Union Congress (TUC) that a State of Emergency was being proclaimed. The Minister for Industry should seek, at his meeting with the EPEA that evening, to find a basis for a settlement of their dispute within the terms of the Pay Code. The Ministerial Committee on Economic Strategy would consider further on the following day the position on oil supplies, in order to enable a decision to be taken about the introduction of petrol rationing and oil allocation. The Committee would also consider whether it would now be desirable to issue ration books to the public.

The Cabinet -

1. Took note, with approval, of the summing up of their discussion by the Prime Minister.

2. Invited the Home Secretary to arrange for the proclamation of a State of Emergency.

3. Invited the Secretary of State for Trade and Industry to lay orders dealing with the restriction of electricity consumption, and to make an appeal for voluntary conservation of fuel supplies, as indicated in the summing up.

4. Invited the Secretary of State for Employment to inform the Confederation of British Industry and the Trades Union Congress that a State of Emergency was to be declared.

5. Invited the Minister for Industry to seek a settlement of the power engineers' dispute within the terms of the Pay Code.

Cabinet Office

14 November 1973
THE CHANCELLOR OF THE EXCHEQUER said that during the previous 3 months the deficit on trade in goods had been running at £150-£200 million a month, but sterling had held up well, and the effect on confidence had been less than had been anticipated. The October trade figures, which would be published that day, would however show a deficit of nearly £300 million. The real deficit would be even greater than this because some imports through Heathrow Airport during the month would not be included in the published figure. Although it could be explained that a number of special factors had contributed to the bad result for October, the effect on confidence would undoubtedly be adverse. Some commentators would press for drastic action, for example in the field of public expenditure or taxation, in order to switch demand into exports. If the trade deficit were to continue at the level prevailing over the last few months, the possibility of action of this kind could not be ruled out, but that would require further consideration. Action to increase taxation would involve considerable difficulties, since changes in direct taxation could not be made effective quickly, whereas increases in indirect taxation, on the scale required to deal decisively with the situation, would raise the retail price index by up to 2 per cent and would thus prejudice the success of Stage 3 of the counter-inflation programme. In order to deal with the immediate problem of confidence, the Bank of England would announce that day an increase of 2 per cent in the level of special deposits, to be called up in four instalments over the period to January 1974. The Bank of England’s minimum lending rate would be increased from 11½ per cent to 13 per cent. The Bank of England were also discussing the situation with the clearing banks, who might decide to increase their base lending rate also to around 13 per cent. Action on these lines might be criticised as putting the whole strain of dealing with the problem on monetary policy, and there might be some fall in the sterling exchange rate; but it was hoped that the action now proposed would be sufficient to maintain confidence and deal with the immediate situation.
THE SECRETARY OF STATE FOR TRADE AND INDUSTRY said that during the second half of October the computer used to calculate the value of imports through Heathrow Airport had been immobilised by a strike. The value of imports during that month which had not yet been counted could be in the range £60-£100 million. As there was a wide measure of uncertainty, he had decided that it would be better to omit this element altogether, rather than to put in an estimated figure which could not be soundly based. The October trade figures had been affected by a number of other special factors. The Middle East war and the stoppage of consignments of diamonds to Israel had resulted in higher imports of diamonds from Russia and lower exports to Israel. Higher imports of oil, and the acceptance of delivery of tankers during the month, had also added substantially to the deficit. The combined effect of these special factors had been to add about £150 million to the normal level of deficit. Apart from this, the value of imports was anyway running considerably higher than a year ago, but this largely reflected higher imports of industrial materials and machinery. The value of imports would now also be permanently increased by the higher price of Middle East oil. Although exports in October were some £60 million down, partly because of the stoppage of diamond shipments, they were still 37 per cent higher than in 1972, and for the first year since the Second World War they were rising faster than world trade. The latest surveys by the Confederation of British Industry also showed that prospects for exports were at record level. The problem at present was not so much one of obtaining export orders as of achieving deliveries. If an improvement could be achieved in deliveries of, for example, motor cars, this would at the same time avoid drawing in foreign products and release home production for export.

In discussion, concern was expressed about the effect which the proposed action might have on the cost of mortgages for house purchase. In the recent discussions with the building societies, it had been hoped that the present 11 per cent rate could be held for some time. If the Bank of England's minimum lending rate was now raised to 13 per cent, there would be widespread dismay among those with substantial mortgage liabilities, who would fear that the mortgage rate would soon rise to a similar figure. This would be an inescapable commitment on their family budget, and the Government would be criticised for allowing the cost of essentials such as food and housing to rise, as compared with non-essential goods such as cigarettes and spirits on which consumers could choose their level of expenditure. Would it have been preferable therefore to contemplate the immediate use of the tax regulator in order to increase the tax on these non-essential items? Alternatively, the use of import deposits might be considered; or might the call for special deposits have to be coupled with a promise of further measures to be introduced shortly? On the other hand, it was argued that because of the risk of forestalling it was not practicable
to foreshadow further measures without specifying what these would be. Import deposits would be contrary to our obligations in the European Economic Community. Increases in direct taxation could not be implemented quickly and would have no immediate effect on demand. Increases in indirect taxes would need to be large enough to deal with the problem without the need for further action later on. This could not be done by touching only non-essential items; it would involve a large general increase in prices which would reduce standards of living and put at risk the success of Stage 3 of the counter-inflation programme, and any consequent industrial trouble would itself tend to frustrate the objective of maintaining confidence. Moreover, a large increase in taxation would disturb those Government supporters who had hitherto been reassured by the Government's commitment to economic expansion. In the short term, therefore, there seemed no escape from the use of monetary measures, which were more flexible and could, if necessary, be quickly adjusted in the light of subsequent developments. To be convincing, such measures must include some immediate action on interest rates. If no statement were made about the minimum lending rate, there would be considerable confusion and it might even rise above 13 per cent as a result of the automatic adjustment of the lending rate in the light of the Treasury Bill tender. It seemed preferable therefore to announce at once the proposed increase to 13 per cent. While it was not expected that, as a result, mortgage interest rates would rise before January, no guarantee could be given about their future level. It would however be desirable to make a statement which would do something to allay the anxieties of householders with existing mortgage commitments.

In further discussion it was suggested that the need for further action in the future would depend on the underlying trend of the balance of trade, which could only be assessed from subsequent monthly trade figures. The prospect would however be worsened by the higher Middle East oil prices, and the breathing space provided by the present measures should be used to consider urgently the other possible measures that might be necessary to redress the balance of payments. The call for special deposits should be backed by selective action on credit, aimed at restricting excessive domestic consumption. The Government would be under pressure to make further cuts in public expenditure, but after the reductions that had already been agreed these would be very hard to find, and the higher level of interest rates would tend to increase public expenditure, particularly in the local government sector. Some increase in taxation might therefore prove necessary. In view of the recent increase in the price of Middle East oil and the difficulties of obtaining supplies, there seemed anyway a strong case for some fiscal action to encourage economy in the use of oil, and it should not be too difficult to secure public acceptance of this
in present circumstances. More effective taxation on capital gains from property development also seemed to be of high priority. Consideration might also be given to the possibility of an increase in the betting tax, although this would not have much effect on demand, and in the rate of tax on non-essential goods. Other possibilities which might be considered were an increase in national insurance contributions, which had the advantage of not affecting the retail price index, and a generous index-linked savings scheme to draw in funds not attracted by the existing savings media.

THE PRIME MINISTER, summing up the discussion, said that in view of the paramount need to ensure the success of Stage 3 of the counter-inflation programme, the Cabinet agreed that the Government’s immediate reaction to the October trade figures should take the form of monetary measures rather than increases in taxation. The Cabinet accordingly endorsed the measures now proposed by the Chancellor of the Exchequer. These should be supported by selective measures of credit control. Concern had been expressed about the possible impact of the higher interest rates on the cost of house mortgages, and while no guarantee could be given about the future movement of mortgage rates, the Chancellor of the Exchequer, in consultation with the Secretary of State for the Environment, should consider what could be said to allay the anxieties of householders with mortgage commitments. The breathing space provided by the present measures should be used to examine the longer-term measures that might prove necessary if the trade deficit continued at its present level. This consideration should include the various fiscal and other measures which had been mentioned in discussion, and particular attention should be given to measures designed to restrain the consumption of oil.

The Cabinet -

Took note, with approval, of the summing up of their discussion by the Prime Minister.

Cabinet Office

14 November 1973