CABINET

CONCLUSIONS of a Meeting of the Cabinet
held at 10 Downing Street on
THURSDAY 14 MARCH 1974
at 10.30 am

PRESENT
The Rt Hon Harold Wilson MP
Prime Minister

The Rt Hon Edward Short MP
Lord President of the Council

The Rt Hon Lord Elwyn-Jones
Lord Chancellor

The Rt Hon Denis Healey MP
Chancellor of the Exchequer

The Rt Hon Michael Foot MP
Secretary of State for Employment

The Rt Hon Shirley Williams MP
Secretary of State for Prices and Consumer Protection

The Rt Hon Anthony Wedgwood Benn MP
Secretary of State for Industry

The Rt Hon Roy Mason MP
Secretary of State for Defence

The Rt Hon William Ross MP
Secretary of State for Scotland.
The Rt Hon Merlyn Rees MP
Secretary of State for Northern Ireland

The Rt Hon Frederick Peart MP
Minister of Agriculture, Fisheries and Food

The Rt Hon Harold Lever MP
Chancellor of the Duchy of Lancaster

The Rt Hon Lord Shepherd
Lord Privy Seal

ALSO PRESENT
The Rt Hon Robert Mellish MP
Parliamentary Secretary, Treasury

SECRETARIAT
Sir John Hunt
Mr H F T Smith (Items 1-4)
Mr P Benner (Items 1, 2 and 7)
Mr J A Hamilton (Items 5 and 6)
Mr J Anson (Item 5)
Mr R J O'Neill (Items 3 and 4)
Mr R L Baxter (Item 6)

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PRICES POLICY

1974 UPRATING OF SOCIAL SECURITY BENEFITS
1. THE PRIME MINISTER said that he had already urged his colleagues to study "Questions of Procedure for Ministers" (C(P)(74) 1) very carefully. He wanted now to emphasise that, although it was important that the Government's policies should be publicly presented to the best advantage, Ministers should exercise caution in agreeing to give interviews to the media, including the foreign press. Ministers who thought it right to give such interviews should normally confine their remarks to matters for which they were directly responsible; in particular, pronouncements should not be made about fiscal questions, matters involving public expenditure or foreign relations (which of course included this country's relationship with the European Economic Community) unless there had been full prior consultation with the responsible Ministers.

The Cabinet -

Took note of the statement by the Prime Minister.

2. The Cabinet were informed of the business to be taken in the House of Commons during the following week.

It was noted that there was a possibility that the Government could be defeated on the amendment to the Address in Reply to the Gracious Speech which the Conservative Party had put down for debate on 18 March, though it seemed doubtful whether either the Conservative or the Liberal Party wished in fact to precipitate an early general election. The situation could in any case be considered at the meeting of the Cabinet which had already been planned for the morning following the debate. In the meantime, it would be useful for the Foreign and Commonwealth Secretary, in a public speech which he would be making on the evening of 15 March, to stress the importance in the national interest that there should be stability in Government at the present time.
FOREIGN AFFAIRS

3. THE SECRETARY OF STATE FOR FOREIGN AND COMMONWEALTH AFFAIRS said that it would be necessary to review our policy on naval visits to certain countries. Pending the outcome of this review a visit to Athens by 2 ships of the Royal Navy which was to have taken place that day had been cancelled. Visits to Portugal would also be suspended, but for practical reasons vessels of the Royal Navy should be allowed to visit the Azores.

THE SECRETARY OF STATE FOR DEFENCE said that, in general, it was desirable to avoid cancelling visits at very short notice. A review of our policy should be conducted jointly by the 2 Departments, and they had agreed that this should be done.

The Cabinet -

Took note of the statements by the Foreign and Commonwealth Secretary and the Secretary of State for Defence.

NORTHERN IRELAND

4. THE SECRETARY OF STATE FOR NORTHERN IRELAND said that the success of the Protestant candidates opposed to the Sunningdale Agreement in winning 11 seats in the General Election had been a severe blow to Mr Faulkner and his supporters in the Northern Ireland Assembly, and had affected morale in the Executive. We must continue to make it clear that the Executive and the principle of power-sharing had our full support. We should continue to work for progress on the Sunningdale Agreement; it would be unwise to yield to pressure from those who were opposed to this.

The Cabinet -

Took note of the statement by the Secretary of State for Northern Ireland.
5. The Cabinet considered a memorandum by the Chancellor of the Exchequer (C(74)4) on public expenditure in 1974-75.

THE CHANCELLOR OF THE EXCHEQUER said that the country confronted an economic situation which might well be the worst which had ever been faced in peacetime, and which was deteriorating. In the past year inflation had been running at over 10 per cent; the balance of payments deficit had been around £1,500 million; the borrowing requirement had been £4,000 million; and growth had virtually come to a halt by the end of the year. In the absence of any change in economic policies, inflation this year would be over 15 per cent; the balance of payments deficit would increase to about £4,000 million, which implied a significant increase quite apart from the deficit arising from higher oil prices; the borrowing requirement would be about £3,000 million; and the prospects for growth were highly uncertain. The 3-day week had multiplied the problems by reducing the gross domestic product by 10 per cent during the first 2 months of the year, with a cut in industrial output of 20-30 per cent. Industry was now short of both money and stocks, and there was great uncertainty about how rapidly the economy would recover. There were also uncertainties about the future trend of commodity prices and the prospects for world trade.

It was clear that there would be no scope for any increase in living standards this year, although there might be some improvement in the second half of the year compared with the present depressed level. The threshold agreements which had been included in Stage 3 of the Conservative Government's Counter-Inflation policy would act as a straitjacket to policy. While not many such agreements had yet been made, they were likely to be generalised, and the 7 per cent threshold level would probably be reached in April, with the agreements being triggered about 9 times during the rest of the year. While this would make it economically virtuous to subsidise the cost of living, it would also limit the Government's freedom of action, particularly in the use of indirect taxation.

Against this background his aim would be to ensure that during a period of sacrifice the burdens would be fairly shared. He would also aim to make the maximum use of manpower and materials to increase growth as rapidly as possible. It would be necessary to shift resources from private consumption into the balance of payments and investment, but not so rapidly as to dislocate the economy and lead to large increases in unemployment. In order to clear the way for his final Budget decisions, it would be necessary to decide the total level of public expenditure by the end of the week. He had already made progress in settling the expenditure on food subsidies, and the Cabinet would be discussing the size of the uprating of social security benefits later in the meeting. On nationalised industry prices, the Cabinet had already agreed to a
substantial increase in the price of industrial coal, and he considered that it would be necessary to accept increases in postal and telecommunication charges and railway fares. The Government would also be faced with a very difficult judgment on steel and electricity prices. On defence, he proposed that the reduction announced by the previous Government of £175 million in 1974-75 should be increased to £250 million; and that an announcement of this should be linked with the intention, announced by the Government when they were last in office, to withdraw from East of Suez except Hong Kong. On the major expenditure projects mentioned in paragraph 6 of his memorandum, he hoped to reach agreement with the Secretary of State for the Environment on a holding position for the Channel Tunnel project, and on a suspension of expenditure on Maplin, at least for the coming year and preferably longer. On the Concorde project, he had circulated a minute to members of the Cabinet setting out the facts, and there was already Parliamentary pressure for these to be disclosed. He hoped that as a first step the facts could be made available publicly. In his view the project should be cancelled, but this was a matter which the Cabinet would need to discuss separately.

He would shortly be putting proposals to the Cabinet for the review of public expenditure programmes for the years from 1975-76 onwards. For 1974-75, he invited the Cabinet to agree that net additions to public expenditure should be limited to those affecting personal incomes and expenditure, as indicated in paragraph 2 of C(74) 4; and that in view of these additional expenditures and the risk of subsidies being needed for the nationalised industries, any other net additions to public expenditure programmes in 1974-75 must be avoided.

General

In discussion, there was general agreement with the approach proposed by the Chancellor of the Exchequer. The limitation proposed on public expenditure in 1974-75 would bear severely on some programmes, particularly those which had been cut by the previous Administration in December. Some Ministers might therefore wish to propose some variation within their total allocation. The Cabinet would however have an early opportunity to discuss the arrangements for reviewing expenditure in 1975-76 and subsequent years; and it might also be appropriate, later in the year, to review public sector building programmes in the light of the prospects for the construction industry. The following further points were also made in connection with particular expenditure programmes.
Concorde

Before a substantive decision was taken on the future of the Concorde project, it should be fully discussed by the Cabinet, who would need not only a statement of the financial costs involved, but also an estimate of the social costs, including unemployment, social security benefits, and retraining. There would be a very strong reaction from the French Government to any proposal for cancellation, and the Attorney General should be asked to advise on the legal position. It was also for consideration whether the final decision should be announced in the Budget or whether, for example, a Select Committee should be appointed. But whatever final decision was reached, there seemed to be overwhelming advantage in revealing the facts at the earliest opportunity after the General Election, as a background to the decisions which the Government would subsequently announce; and the French Government could not reasonably object to this since they had recently themselves issued a Press statement unilaterally. It would be desirable to give advance warning to the French Government, the manufacturers and the trades unions that a statement of the facts was being issued. The statement might give rise to a demand for an immediate Debate, but in that case the Government should avoid commenting on the substance and take credit for having brought the facts to light. The way in which the matter should be handled in the Budget should be further considered in the light of public reaction to the statement.

Channel Tunnel
Maplin Airport

Proposals for the future of the Channel Tunnel and Maplin Airport projects would shortly be brought before the Cabinet. Full account would need to be taken of the effect on other airports if Maplin was not built.

Defence

The Secretary of State for Defence would co-operate with the Chancellor of the Exchequer in seeking ways of achieving the additional reduction which he had proposed. It would however not be easy because reductions, whether in manpower or in equipment projects, tended in the short run to entail additional expenditure on redundancy payments and cancellation charges. Moreover, while an announcement about withdrawal from East of Suez might help to strengthen the credibility of the expenditure cuts, it would be unwise to take this step without proper consultation, which might take another 2 or 3 weeks.
Agriculture

There would be particular problems in regard to agriculture, given that the Government was committed to expansion and that our farmers were getting lower prices than in the original member countries of the European Economic Community, but were faced with large increases in the cost of feeding-stuffs. The Government's commitment was however limited to the maximum economic expansion of agriculture, and there was room for argument as to the level of expansion that could be considered economic.

Education

The December reductions in the education programme could lead to some limitation of teacher establishments, with the result that a number of teachers leaving training colleges might not find employment. The reduction of 20 per cent in capital expenditure during the year would require a reduction of 50 per cent in new starts, so that the school building programme would be limited to accommodating increased numbers in areas where the school population was expanding. The inner city areas, which were particularly deserving of help, would therefore suffer disproportionately. While at the present time there was no room for reversal of any of the December cuts, the matter might be reviewed later in the year in any general review of construction programmes.

Nationalised Industry

Increases would be needed in postal and telecommunications charges. A decision on steel prices would be more difficult, and needed further consideration. In the electricity industry, the forecast deficit was now around £500 million, and an increase would be proposed taking due account of the possible effect on threshold agreements. Where increases were proposed for domestic consumers, the Ministers concerned should consult the Secretaries of State for Prices and Consumer Protection and for Social Services on the implications for the low-paid and pensioners. Even with the increases in supplementary benefits which were now being proposed, an increase in supplementary heating allowances was likely to be necessary to offset higher bills for electricity and paraffin; and if some help of this kind could be given it might enable larger general price increases to be made. There was a case for placing most of the burden of the price increases on industry, since our exports appeared at present to be underpriced in export markets. Nevertheless, industry also faced considerable liquidity problems; and the most important problem to be tackled at present was inflation, which was more serious here than in our main competitor countries. By the end of the year, we might again be becoming uncompetitive in export markets, and a policy of increasing industrial costs to achieve a temporary increase in export prices could therefore be damaging.
A choice would however need to be made between the various ways of allocating the price increases, given that, at the margin, an increase in one sector released funds for subsidies elsewhere.

THE PRIME MINISTER, summing up the discussion, said that the Cabinet endorsed the broad approach proposed by the Chancellor of the Exchequer in C(74) 4. Individual Ministers should discuss the detailed implications for their programmes with the Chief Secretary, Treasury, as necessary. The Cabinet would be considering later in the meeting the proposals regarding the uprating of social security benefits. It was important that no proposals for increased expenditure should be revealed before the Chancellor of the Exchequer was able, in his Budget statement, to demonstrate how they would be financed. The Cabinet would need to give early consideration to the future of the Concorde project, Channel Tunnel and Maplin Airport, in the light of memoranda circulated by the Ministers concerned, which should take account of the social as well as the economic implications. In the meantime, the Cabinet agreed that the Secretary of State for Industry should release a statement of the facts concerning the Concorde project for public discussion. A draft of this statement should be cleared with himself and with the Lord President, the Foreign and Commonwealth Secretary, the Chancellor of the Exchequer and the Attorney General; and prior warning of its issue should be given to the French Government, and the manufacturers and trades unions. The Cabinet would consider at a later meeting the arrangements for preparation of public expenditure programmes for 1975-76 and thereafter; and noted that it might be desirable to review public sector building programmes later in the year, in the light of the prospective level of demand on the construction industry.

The Cabinet -

1. Approved the recommendation in paragraph 3 of C(74) 4.

2. Invited the Secretary of State for Industry -

   a. To issue a statement of the facts of the Concorde project, as indicated by the Prime Minister in his summing up.

   b. In consultation with the Foreign and Commonwealth Secretary, the Chancellor of the Exchequer, the Secretary of State for Employment and the Attorney General, to circulate a memorandum on the Concorde project for consideration by the Cabinet.
3. Invited the Secretary of State for the Environment to circulate memoranda on the future of the Channel Tunnel and Maplin Airport.

4. Invited the Chancellor of the Exchequer to circulate a memorandum on arrangements for preparation of public expenditure programmes for 1975-76 and later years.

6. The Cabinet considered a memorandum by the Secretary of State for Prices and Consumer Protection (C(74) 5) on prices policy.

THE SECRETARY OF STATE FOR PRICES AND CONSUMER PROTECTION said that she sought the agreement of her colleagues to the urgent preparation of a Bill giving powers to:

i. authorise expenditure on subsidies,

ii. prescribe prices and margins for subsidised goods,

iii. prescribe prices and margins for certain other essential foods,

iv. vary decisions of the Price Commission,

v. require prices to be displayed and goods to be marked with unit prices.

In considering the payment of subsidies she had been obliged to reject the idea of operating through the mechanism of the Value Added Tax; this would have required the rewriting of a computer programme which would have taken months to complete. She had decided to concentrate on certain essential foods and to use existing mechanisms as far as possible. She proposed therefore to subsidise bread and milk, both of which were weighted heavily in the retail price index (RPI); also cheese, butter and sugar, in spite of certain difficulties that would arise in relation to the European Economic Community. She would like to add one other protein food to the list and was investigating the possibilities of eggs, bacon or ham. It would be necessary to introduce the subsidy on bread immediately in order to forestall a price increase. The other subsidies would be announced in the Budget. The cost would be in the region of £400 million a year, excluding the existing milk subsidy. The total would depend mainly on the cost of holding bread prices at the present level. She thought it right to retain the Price Commission as an independent agency to control prices in accordance with a general price code, as it would be unwise to involve the Government
in the detailed control of prices; but she proposed to initiate statutory consultation on three amendments to the Code: first to impose a general reduction of 10 per cent on all distributors' gross margins; secondly to impose a minimum period of three months between price increases; and thirdly if possible to deal with price increases on existing stocks. She would aim to bring the Bill, the subsidies and the amendments to the Price Code into effect more or less at the same time in April. In the longer term she would like to reconsider the provision for allowable costs in the Price Code, and to consider whether the presentation of company accounts could be made to distinguish between profits on home sales and on exports. The proposed amendments to the Price Code had been deliberately stated in uncompromising terms. The Confederation of British Industry and the Retail Consortium would object strongly to some of them, and it might be necessary to offer some concessions in order to get the proposals through Parliament. There might in particular be a real case for allowing some exemptions for the sake of investment; the more tightly gross margins were squeezed the more necessary such exemptions would become.

THE PRIME MINISTER said that he had held a meeting the previous day to discuss the abolition of the Pay Board. The meeting had agreed that the power to abolish the Pay Board should be included within this Bill. The prospects of Parliamentary approval seemed better at present than they might be later and the provision would improve the prospects for the negotiations with the Trades Union Congress on a voluntary incomes policy. The clause would however be drafted in such a way that its deletion in Parliament would not damage the rest of the Bill. It would enable the Secretary of State to abolish the Pay Board by means of an order requiring an Affirmative Resolution of the House, and it would be made clear that this would not be done until some progress had been made in working out a voluntary policy.

In discussion it was argued that the public would expect a more general introduction of cash margin controls. They would also expect action on sharp increases in the prices of foods such as spaghetti which might not be regarded as essential foods. Against this it was argued that the control of prices and margins would have to be limited to a small number of essential foods in order to enable the firms to cover their losses by cross-subsidisation from their profits on other foods. The proposed 10 per cent cut in margins would be reinforced where necessary by the use of paragraph 80 of the Price Code, which enabled the Commission to recommend a reduction in margins where the cost of any goods rose substantially. The costs of the whole policy would have to be borne by industry, which was already facing cash flow difficulties and deferments of investment. Many firms, particularly manufacturers hit by frequent increases in world prices, would need to take advantage of any provisions for special exemption.
In further discussion it was argued that the principal short-term aim should be to delay the first triggering of the threshold agreements; there was a danger of two triggerings in April. However, the subsidies could reduce the RPI by only 1 per cent and it would be necessary to look for other ways to moderate or at least to delay increases in the cost of living. In presenting these measures to the public, Ministers would have to make it clear that they could do no more than moderate the price increases which would otherwise have taken place. It would be rash to set any particular target, as economists differed widely in their judgements about the rate of price increases that could be expected over the next few months. In the longer run there was still the possibility of downturn in commodity prices.

The following points were made in further discussion -

a. It was illogical to deal separately with the milk subsidy, which should now be treated as a consumer subsidy like the rest. If the milk subsidy were brought within the Bill it would be necessary to raise the financial ceiling to accommodate it.

b. Although the whole Bill should apply to Northern Ireland it would be reasonable to make the Northern Ireland Executive responsible for the powers in ii., iii. and v. of the statement by the Secretary of State for Prices and Consumer Protection.

c. Although the existing Price Code exempted steel because of our obligations under the European Coal and Steel Community, it would be desirable if possible to control steel prices, particularly the price of tinplate which featured heavily in consumer expenditure.

THE PRIME MINISTER, summing up the discussion, said that the Cabinet agreed that the Secretary of State for Prices and Consumer Protection should set in hand urgently the preparation of a Bill on the lines proposed in her paper, with the addition of an enabling clause for the abolition of the Pay Board. She should consult further with the Chancellor of the Exchequer and the Minister of Agriculture, Fisheries and Food about the inclusion of the milk subsidy; and with the Secretary of State for Northern Ireland about the powers to be assigned to the Northern Ireland Executive. It would also be helpful if she would circulate a note to her colleagues giving the answers to questions that they might be asked about the proposals: in particular, why there were to be no subsidies on meat, chicken, or fish. It would be desirable to re-examine the policy on price control and subsidies during the summer in the light of the movement of commodity prices.
The Cabinet -

Took note with approval of the summing up of their discussion by the Prime Minister and invited the Secretary of State for Prices and Consumer Protection to be guided accordingly.

7. The Cabinet had before them a memorandum by the Secretary of State for Social Services (C(74) 6) about the 1974 uprating of social security benefits.

THE SECRETARY OF STATE FOR SOCIAL SECURITY said that the Government were committed by the Election Manifesto to increase pensions to £10 for single people and £16 for married couples. At the time when her memorandum had been circulated two points had been outstanding - the method of financing the uprating and the date from which the increases should be implemented. On the first point, she had now been able to reach agreement with the Chancellor of the Exchequer. For reasons of demand management he had found it necessary, despite the substantial surplus at present in the National Insurance Fund, to seek substantial increases in contributions. Agreement had been reached on arrangements which would protect the least well paid by imposing progressively heavier burdens on the better off. There would be a substantial increase in the flat rate contribution payable by employers. So far as employees were concerned, the flat rate contribution would be reduced but there would be substantial progressive increases in the earnings related contributions. The overall effect was that the contributions payable by those earning less than £25 a week would be slightly reduced while the contributions payable by those earning more than that amount would be progressively increased by amounts rising to a maximum of 57p at the proposed new earnings ceiling of £62 a week.

So far as the date of implementation was concerned, it was important, in view of the Manifesto commitment, that there should be no avoidable delay. The earliest date which was administratively possible was 22 July, and this should be accepted as the objective. The Social Policy Committee of the Trades Union Congress (TUC) had, at a recent meeting with her, indicated that they hoped for implementation in April; and deferment until October, which was the date preferred by the Chancellor of the Exchequer, would cause great disappointment. In the interests of early implementation she had decided not to propose increases in a number of benefits which were urgently in need of review. But in its progress through the House of Commons the Bill would be open to amendment to secure improvement in these benefits, and it might be difficult to resist
such amendments except on the ground that the Bill had been drafted in such a way as to make possible implementation at the earliest possible date. Moreover, deferment of the operative date until the autumn would mean that by October 1975 pensioners would be little better off under the Government's scheme than they would have been under the proposals put forward in the Conservative Party's Election Manifesto, which involved six-monthly uprating.

In discussion, it was argued that in order to protect those who had low incomes but did not qualify for supplementary benefit, it would be necessary to make improvements in the rent and rate rebate schemes; and this would represent a further significant net addition to public expenditure. A still further addition, of the order of £80 million, would come from the payment later this year of the £10 Christmas bonus to the continuance of which the Labour Party had committed itself.

In further discussion, it was argued that there were strong financial reasons for preferring implementation in October. The extra cost of implementation in July was very considerable - it would in fact be the equivalent of an addition of about 1p to the standard rate of income tax. Uprating would moreover have an unfavourable effect on the retail price index, which it was desirable to defer as long as possible. It also could not be overlooked that it might well prove impossible in the event of an uprating in July to hold the position that there should be no further uprating until October 1975. The position was made all the more difficult by the additional expenditure arising from the Christmas bonus and likely changes in the rent and rate rebate schemes. There was in fact no commitment to implementation before the autumn; and although there would no doubt be disappointment that immediate implementation was administratively impossible, it was doubtful whether October would produce a significantly more unfavourable reaction than July. An interim date however - for example, 1 September - had little merit: its financial benefits would be relatively small, but it would not be early enough to satisfy those wanting very rapid implementation.

On the other hand, it was argued that the uprating of pensions had been firmly identified as the Government's first priority. The fact that it was to be put into effect at the earliest moment which was administratively possible would be of great help in the discussions with the TUC on voluntary arrangements for dealing with pay; and it would make easier the continuance of the Pay Board until a satisfactory agreement had been reached on voluntary arrangements. Moreover, the possibility of an early Election made it very desirable that the Government should be able to show that they had acted as rapidly as possible to give effect to their undertaking to increase pensions. In any event it was publicly known that implementation by the end of July was administratively possible; and there would
be great difficulty in explaining the reasons for any delay beyond that date. If, however, 22 July were to be achievable, an immediate decision was needed because the necessary arrangements would have to be put in hand at once.

THE PRIME MINISTER, summing up the discussion, said that the Cabinet approved the proposals which had been worked out for financing the proposed uprating of pensions and congratulated the Ministers concerned on the ingenious solution which had been found. As regards timing, the Cabinet agreed on balance that the new rates should be payable from 22 July rather than from a date in October, in view particularly of the assistance that an early date would give to the discussions with the TUC on voluntary arrangements for pay. But the Cabinet recognised that implementation in July might oblige the Chancellor of the Exchequer to seek a higher increase in taxation and greater reductions in some areas of public expenditure than would otherwise have been necessary; and he was entitled to expect co-operation from his colleagues if further expenditure reductions in fact proved necessary. The Cabinet's decisions would be announced by the Chancellor of the Exchequer in the context of the Budget; and the Secretary of State for Social Services should put in hand the steps needed to secure implementation on 22 July, including the preparation of legislation.

The Cabinet

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