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CM(76) 34th
Conclusions

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CABINET

CONCLUSIONS of a Meeting of the Cabinet
held at 10 Downing Street on

THURSDAY 25 NOVEMBER 1976

at 10.30 am

PRESENT

The Rt Hon James Callaghan MP
Prime Minister

The Rt Hon Michael Foot 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 Anthony Crosland MP
Secretary of State for Foreign and Commonwealth Affairs

The Rt Hon Merlyn Rees MP
Secretary of State for the Home Department

The Rt Hon Shirley Williams MP
Secretary of State for Education and Science and Paymaster General

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

The Rt Hon Eric Varley MP
Secretary of State for Industry

The Rt Hon Peter Shore MP
Secretary of State for the Environment

The Rt Hon Roy Mason MP
Secretary of State for Northern Ireland

The Rt Hon Bruce Millan MP
Secretary of State for Scotland

The Rt Hon John Morris QC MP
Secretary of State for Wales

The Rt Hon Fred Mulley MP
Secretary of State for Defence

The Rt Hon Albert Booth MP
Secretary of State for Employment

The Rt Hon David Ennals MP
Secretary of State for Social Services

The Rt Hon Edmund Dell MP
Secretary of State for Trade

The Rt Hon Lord Peart
Lord Privy Seal

The Rt Hon John Silkin MP
Minister of Agriculture, Fisheries and Food

The Rt Hon Roy Hattersley MP
Secretary of State for Prices and Consumer Protection,

The Rt Hon William Rodgers MP
Secretary of State for Transport

The Rt Hon Stanley Orme MP
Minister for Social Security

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

The Rt Hon Reginald Prentice MP
Minister for Overseas Development

ALSO PRESENT

The Rt Hon Michael Cocks MP
Parliamentary Secretary, Treasury
(Items 1 and 3)

SECRETARIAT

Sir John Hunt
Mr G R Denman (Item 2)
Mr W I McIndoe (Item 1)
Mr D le B Jones (Item 3)
Mr J A Marshall (Item 3)
Mr A D Gordon-Brown (Item 1)
Mr A K H Atkinson (Item 2)

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PARLIAMENTARY AFFAIRS

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

THE LORD PRESIDENT OF THE COUNCIL said that the business on Wednesday 1 December would be the Second Reading of the Aircraft and Shipbuilding Industries Bill, and a related procedural Motion the precise form of which was still under consideration. This Motion would need to cover both the truncation of the Committee and Report Stages, as had been done in the previous Session with the Trade Union and Labour Relations (Amendment) Bill, and the question of hybridity. Unless the Government indicated their intention of putting down a Motion to the effect that the Bill should proceed as a public Bill, then the Bill would - under the normal procedure of the House - be referred to the Examiners for them to consider whether it was hybrid, a process which would take two weeks or more. Meanwhile it would not be possible to proceed with Second Reading so that, even assuming the Bill was found not to be hybrid, Second Reading would be delayed until after the Christmas Recess. The provisions now alleged to be hybrid were those relating to ship-repairing, not those on which the Speaker had given his ruling of prima facie hybridity last May. If the Examiners found that the Bill was hybrid, it would then be referred to a Select Committee, which would hear any petitions against provisions of the Bill and which might make amendments. Parliamentary proceedings on the Bill would then drag on for many months. He hoped that the procedural Motion could be taken after Second Reading on 1 December, but this might not be possible if the question of hybridity were to be raised in the House before then. The Motion might provoke a considerable row with the Opposition but this could not be helped.

In discussion it was pointed out that the debates on the Aircraft and Shipbuilding Industries Bill on 1 December, and on the Second Reading of the Social Security (Miscellaneous Provisions) Bill on 2 December, would mean taking two difficult and contentious pieces of business immediately after the Debate on the Address, which would sour the atmosphere at the start of the new Session. It was, however, important to make early progress on both Bills, and there might be difficulty in obtaining Second Reading for the Social Security (Miscellaneous Provisions) Bill; the Government's majority was likely to be reduced from Monday 6 December. The procedural Motion on the Aircraft and Shipbuilding Industries Bill could be justified on the basis that hybridity should not be used as a device to frustrate the operation of the Parliament Act; and a row with the Conservatives on this Bill on 1 December might help with the morale of backbenchers, and reduce the risk of defections in the vote the following day on the Second Reading of the Social Security (Miscellaneous Provisions) Bill. While those backbenchers who had previously voted against the Government on the earnings rule for retirement pensioners were now believed to recognise that the alternative to the Government's proposal to restrain a further rise in the earnings rule would be even worse, there was considerable opposition to the proposal to restrict payment of unemployment benefit to occupational pensioners. There could be no question of forgoing this saving of unemployment benefit, though it might be possible to offer the prospect of some give in Committee. While further time for consultation with the Parliamentary Labour Party might help to reduce the risk of failing to carry the Second Reading of the Social Security (Miscellaneous Provisions) Bill, there was no other suitable business to bring forward to 2 December; and it would have to be emphasised to the Party that the alternative to the Government's policies was a Conservative Government.

THE PRIME MINISTER, summing up the discussion, said that the Cabinet accepted the need to take the Second Reading of the Aircraft and Shipbuilding Industries Bill and the related procedural Motion, and the Second Reading of the Social Security (Miscellaneous Provisions) Bill, in the following week. It was important to do everything possible to ensure that the latter Bill would receive a majority on Second Reading.

The Cabinet -

Took note.

CAP STRATEGY

Previous Reference: CM(76) 9th Conclusions, Minute 2

2. The Cabinet had before them a memorandum by the Secretary of State for Foreign and Commonwealth Affairs (CP(76) 112) covering a report by the Ministerial Committee on European Questions on a strategy for the Common Agricultural Policy (CAP).

THE FOREIGN AND COMMONWEALTH SECRETARY recalled that the Cabinet at their meeting on 11 June had expressed the wish to consider before the end of the year our strategy towards the CAP. The Ministerial Committee on European Questions had in the first instance remitted the question to a small Sub-Committee of the Ministers mainly concerned, chaired by the Minister of Agriculture, Fisheries and Food. After considering the Sub-Committee's report the Ministerial Committee were agreed in recommending that our long-term aim should be to eliminate structural surpluses by reducing Community support prices, but that in the medium and short term we should give priority to retaining for as long as possible the very substantial advantages we derived from the Green Pound and should give up no more of those advantages than was necessary to secure an acceptable price settlement.

In discussion there was general agreement with the recommendations of the Ministerial Committee. In the short term we were in a stronger position to retain the benefits of the Green Pound than to resist Community price increases. It could be argued that we could not expect to retain those benefits much longer and should make a virtue of necessity by sacrificing them in favour of insistence on a price freeze for surplus commodities. But this was to underrate our ability to hold the Green Pound against pressure both from the Community and from our own agricultural industry, and it was necessary to recognise that an outright confrontation with our partners over prices would be unprofitable. It was however important to be sure of avoiding more than a minimal change in the Green Pound during our Presidency. In the longer term particularly as and when currencies became more stable there would be great pressure from the Community to abolish green currency differentials and we should not lose sight of the bargaining counter this would give us in holding down prices for surplus commodities. Even at the next price fixing we should pursue this aim by all means short of outright confrontation. But it was not clear how far in practice concessions on the Green Pound could be used to secure restraint on prices and we should make no such concessions that were not fully justified by the need for an acceptable price settlement. There were good reasons for believing that the Commission's proposals for automatic adjustment of green currencies could be successfully resisted.

In further discussion attention was drawn to the damaging consequences of the Green Pound for Northern Ireland where agricultural employment was much more important than in Great Britain and where there was serious unemployment in rural areas. The green currency differential in favour of the Republic resulted in widespread smuggling of livestock to the South and it had been necessary to subsidise supplies to Northern Ireland meat plants at a cost of £1 million per month. This was a burden which should be shared by the United Kingdom.

THE PRIME MINISTER, summing up the discussion, said that the Cabinet noted the special problems of Northern Ireland, but accepted the recommendations of the Ministerial Committee on European Questions set out in the report attached to CP(76) 112, subject in particular to our taking as tough a line in next year's fixing of Community prices as was compatible with the avoidance of confrontation and to our only making concessions on the Green Pound which were fully justified by an acceptable price settlement.

The Cabinet -

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

IMF NEGOTIATIONS

Previous Reference: CM(76) 33rd Conclusions, Minute 2

3. The Cabinet resumed their discussion of the negotiations with the International Monetary Fund. Their discussion and the conclusions reached are recorded separately.

Cabinet Office

25 November 1976

TOP SECRET

Copy No. 38

CABINET

LIMITED CIRCULATION ANNEX

CM(76) 34th Conclusions, Minute 3

Thursday 25 November 1976 at 10.30 am

IMF NEGOTIATIONS

Previous Reference: CM(76) 33rd Conclusions, Minute 2

THE PRIME MINISTER said that the action agreed upon at the previous Cabinet discussion had been taken. He had sent messages to President Ford of the United States and to Chancellor Schmidt of West Germany; and both he and the Chancellor of the Exchequer had seen the leader of the International Monetary Fund (IMF) team. The IMF now fully understood that the Cabinet were not convinced of the need for deflationary measures; and they understood the nature of the dilemma facing the Government in which if the action taken were unduly severe the Government would lose the present co-operation of the trade unions, whereas if it were too mild it would fail to carry conviction in the markets. Contrary to their previous view, neither Germany nor America were now pressing for an immediate agreement with the IMF, and it was therefore not necessary to push matters to a conclusion in the present week. He himself would be attending the European Council on Monday and Tuesday of the following week, so that Cabinet would resume their discussion of this subject on Wednesday 1 December. In the meantime, officials of the Treasury and the IMF were examining the implications of three possible scenarios, involving differing levels of the Public Sector Borrowing Requirement (PSBR) at £8½ billion, £9 billion and £9½ billion in 1977-78. He had spoken, on Privy Counsellor terms, to Mr Len Murray of the Trades Union Congress (TUC) to indicate the broad nature of the problem to him, and Mr Murray would be giving the matter further thought.

In discussion it was argued that it would be important, when the Cabinet returned to this subject the following week, to have proposals circulated on paper in advance of the meeting so that Ministers would have an opportunity to reflect upon them before the discussion. Indeed, it would be wrong if the sole proposals before Cabinet were those which the Prime Minister and the Chancellor of the Exchequer had at the last meeting said they would hope to put forward jointly. It would not be enough for Cabinet to be asked to approve or reject one set of proposals. There should be an opportunity to discuss alternative courses, including the more radical alternative strategy which had already had some discussion in the Ministerial Committee on Economic Strategy. The Cabinet ought also to discuss the likely content of the Letter of Intent which the IMF would need; and it was pointed out that the 1975 letter gave an assurance that the Government would not adopt the kind of import restrictions which were at the heart of the alternative strategy. One possible course of action would be to impose a wage and price freeze for a period - although it was pointed out that, while it might be possible to freeze incomes, most prices were determined by forces which were beyond the Government's control. The Cabinet had, at their last meeting, broadly agreed that there were no economic grounds justifying large deflationary moves; but there had been some support for the view that some reduction in the PSBR would be necessary to reach an agreement with the IMF and thus obtain the loan which was needed to get through the next 12 months. The Government were subject to two constraints: on the one hand it was necessary to satisfy the IMF, and perhaps more important to satisfy the markets, since unless this were done even an agreement with the IMF would be of little value: on the other hand, there was the need to arrive at a package for which the Government could command support in their own Party and in the House of Commons. On the former count, it was argued that the alternative strategy was quite impracticable, and that it was essential to avoid negotiating the IMF into agreeing a package which the markets would reject as inadequate. On the latter count it was argued that any package which involved cuts in public expenditure and a continuation of the rising trend in unemployment would not work, and would destroy the social contract.

In further discussion the following points were made -

a. Market confidence depended not on securing the short-term approval of the Press and others but on having sound policies and economic structures with a good political backing. The establishment of a safety net under the sterling balances would be a major boost for confidence.

b. The announcement of an agreement with the IMF would now be not very widely separated in time from the publication of the economic forecast. There was therefore a strong case for announcing, along with the loan agreement, measures to reduce unemployment in 1977, particularly the extension of the Temporary Employment Subsidy, which placed a lower burden upon the Exchequer than the cost of redundancies. Unless action was taken on unemployment, the social contract would collapse.

c. Time would be needed, after the Cabinet had considered the Chancellor of the Exchequer's proposals the following week, so that once the magnitude of the total public expenditure cut envisaged was settled, there could be a round of discussion with the TUC about its allocation.

d. The IMF had now abandoned the concept of a target for the PSBR in 1978-79, having been persuaded that the uncertainties in such a calculation were too great; and they were moving towards the concept of a target figure for the adjustment, which would be varied in relation to growth. It was suggested that if the target in 1977-78 were £8½ billion, the carry-through of the expenditure cuts that would involve, including the consequential reduction in debt interest, combined with acceptance of the Chancellor of the Exchequer's proposals on export credit, would mean that relatively little further expenditure savings would be needed.

e. It should not however be assumed that, for 1978-79, part of the solution could be found in a hardening of the terms of our export credits. The proposals which had been put forward, but not yet discussed, could mean putting the interests of manufacturing industry second to other considerations. This would finally and totally undermine the Government's industrial strategy.

f. It would be important not to underrate the political realities of the situation. The Cabinet's decision over safety representatives had, as predicted, upset the TUC. The miners, contrary to expectations, were displaying militancy over the early retirement issue - and might, indeed, be trying to move towards free collective bargaining. The Parliamentary Labour Party was likely to prove difficult over the proposal to restrict the right of occupational pensioners to draw unemployment benefit. It was not impossible that the insistence of the IMF on hard terms could lead to the Government losing office.

g. While it would be difficult to carry the Labour Party in a tough package, it might well prove even more difficult to carry them in a repeated series of smaller doses made necessary because the market was unconvinced by the adequacy of the original prescription. It was essential to ensure that any course which was chosen would in fact work in practice.

h. The position was that the country had been spending, and continued to spend, more than it earned. This was true both of the nation and of the Government. In recent years, the real value of the spending of those on social security benefits had been protected by law, while the real incomes of those in work had been cut. A continuation of this could destroy the Labour Party. The seminal issue was that in an economy which was both mixed and open, dependent upon the level of world trade, to spend more than was earned meant that the country became dependent upon foreign borrowing, and thus dependent upon the judgment of those who financed the purchase of British goods and would finance the loan now being sought. It would be essential to convince the Government's supporters that these were facts of life which had to be faced.

THE PRIME MINISTER, summing up the discussion, said that none of the courses facing the Cabinet was attractive or certain in its effect. In the following week they would need to decide which course was least unpalatable and least risky, and then seek the maximum support for it. He understood the desire expressed by some members of the Cabinet for a discussion of an alternative strategy of protection, although it had to be borne in mind that if no agreement were reached on the IMF loan the prospect of an arrangement to deal with the sterling balances, which now seemed very good, would also disappear. The alternative strategy had however hitherto only been discussed in the Ministerial Committee on Economic Strategy and it would be right for the Cabinet to discuss this, in addition to resuming their discussion of the IMF negotiations, in the following week. He would arrange for the circulation of the necessary papers, having regard to the sensitive nature of some of the possibilities envisaged.

The Cabinet -

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

Cabinet Office

25 November 1976