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Conclusions

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CABINET

CONCLUSIONS of a Meeting of the Cabinet
held at 10 Downing Street on
THURSDAY 14 JULY 1988
at 10.00 am

P R E S E N T

The Rt Hon Margaret Thatcher MP
Prime Minister

The Rt Hon Sir Geoffrey Howe QC MP
Secretary of State for Foreign and
Commonwealth Affairs

The Rt Hon Nigel Lawson MP
Chancellor of the Exchequer

The Rt Hon Lord Mackay of Clashfern
Lord Chancellor

The Rt Hon Douglas Hurd MP
Secretary of State for the Home Department

The Rt Hon Peter Walker MP
Secretary of State for Wales

The Rt Hon George Younger MP
Secretary of State for Defence

The Rt Hon Norman Fowler MP
Secretary of State for Employment

The Rt Hon Tom King MP
Secretary of State for Northern Ireland

The Rt Hon Nicholas Ridley MP
Secretary of State for the Environment

The Rt Hon Lord Young of Graffham
Secretary of State for Trade and Industry

The Rt Hon Kenneth Baker MP
Secretary of State for Education
and Science

The Rt Hon Kenneth Clarke QC MP
Chancellor of the Duchy of Lancaster

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

The Rt Hon Malcolm Rifkind QC MP
Secretary of State for Scotland

The Rt Hon Paul Channon MP
Secretary of State for Transport

The Rt Hon John Moore MP
Secretary of State for Social Services

The Rt Hon John Wakeham MP
Lord President of the Council

The Rt Hon The Lord Belstead
Lord Privy Seal

The Rt Hon Cecil Parkinson MP
Secretary of State for Energy

The Rt Hon John Major MP
Chief Secretary, Treasury

THE FOLLOWING WERE ALSO PRESENT

The Rt Hon David Waddington QC MP
Parliamentary Secretary, Treasury

The Rt Hon Peter Brooke MP
Paymaster General

SECRETARIAT

Sir Robin Butler
 Mr R T J Wilson (Item 4)
 Mr R G Lavelle (Item 3)
 Mr P J Weston (Item 3)
 Mr A J Langdon (Items 1 and 2)
 Mr G Monger (Item 4)
 Mr S S Mundy (Items 1 and 2)

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PARLIAMENTARY
AFFAIRS

1. The Cabinet were informed of the business to be taken in the House of Commons in the following week and that, subject to the progress of business, the House would rise for the Summer Adjournment on Friday 29 July until Wednesday 19 October.

HOME AFFAIRS

Rover Group

Previous

Reference:

HC(88) 18.4

2. THE SECRETARY OF STATE FOR TRADE AND INDUSTRY said that the European Commission had on the previous morning agreed the terms on which they would be prepared to approve the sale of the Government's shareholding in Rover Group to British Aerospace plc (BAe), but at the last minute BAe had asked for more time to consider the implications of the conditions attached to the Commission's decision. In particular, BAe had expressed concern that, in the event of any significant departure from the expenditure programme forecast in the Rover Group corporate plan (which BAe had already endorsed), the Commission would have the legal right to demand repayment of the entire sum which the Government was proposing to inject into the Rover Group. BAe directors had said that they would not be prepared to recommend to their shareholders that the company should carry that risk. While the Commission were unlikely to challenge any changes to the corporate plan unless they amounted to a significant departure and, in that event, could be expected to react sympathetically if there were convincing reasons, it was clear that neither the Commission nor the Government could possibly accept a situation under which BAe effectively had carte blanche to depart from the corporate plan. It was not clear whether BAe were simply being naive in putting forward this proposal or whether they were instead seeking a means of resiling from a deal which they no longer regarded as advantageous. BAe should have been aware of the position from the outset and it was extraordinary that they should wait until the very last moment before raising these doubts. The United Kingdom Permanent Representative to the European Community was having a meeting with Commissioner Sutherland to establish what assurances could be given to the directors, and he himself would be meeting BAe directors later that day when it was likely to become clear whether there remained a prospect of reaching an agreement within the terms of the Commission's decision. If it became apparent that there was no prospect of reaching a settlement, it would be important for the Government to make a statement in Parliament as soon as possible in order to seize the initiative from BAe who would no doubt seek to blame the Government for any breakdown. In the event of such a breakdown, it would be essential to ensure that confidence in Rover was preserved, and to seek to discourage any unwelcome bids for the Rover Group from rival car-makers, especially since August was the peak month for sales of new cars. He proposed accordingly that the Government should make clear that their objective remained to return the Rover Group to the private sector within the lifetime of the present Parliament and that he would be exploring the options for securing this with the management of the Group. The performance of the Rover Group had recently much improved and the Group was likely to remain attractive to prospective purchasers.

In discussion, it was noted that it would be wrong to cut short any negotiations which could preserve the sale to BAe simply in order to make a firm statement to Parliament. If the directors required assurances that the Commission would behave reasonably in monitoring the observance of the Corporate plan, such assurances could probably be obtained. But if BAe were insisting that they should be free to depart from fundamental aspects of the Corporate plan or were seeking a pretext for resiling from an agreement which they no longer wanted to pursue, it would be preferable to conclude discussions as soon as possible and retain the initiative in presenting the Government's view.

THE PRIME MINISTER, summing up the discussion, said that the further negotiations which the Secretary of State for Trade and Industry would be holding with BAe should not be foreclosed while there remained any realistic prospect of success, but if it became clear that there was no prospect of reaching a settlement he should make a statement on the matter in the House of Lords at the earliest opportunity. In the event of a breakdown of discussions with BAe, it would be crucially important to ensure that confidence in the Rover Group was maintained. The Cabinet agreed that in that event the Government should make clear that its objective remained to return the Rover Group to the private sector within the lifetime of this Parliament and that it would be discussing with the Group the options for securing this.

The Cabinet -

1. Took note, with approval, of the Prime Minister's summing up of the discussion and invited the Secretary of State for Trade and Industry to be guided accordingly.

Piper Alpha
North Sea
Oil Platform
Explosion

Previous
Reference:
CC(88) 24.2

THE SECRETARY OF STATE FOR ENERGY said that progress continued with securing the remaining structure of the damaged Piper Alpha platform but that the work had been hampered by bad weather. At least three of the six oil wells on the site were not under control, and the priority task was to cut the flow of oil and gas from them. Oil pollution was being carefully monitored and was very slight. A few further bodies had been recovered during the previous week, but the bodies of most of the victims were probably trapped in the remains of the platform's living accommodation which had sunk. He had set up a public inquiry into the incident and, having consulted the Lord Advocate and the Lord Chancellor, had appointed Lord Cullen as its chairman. This appointment, in which he had complete confidence, had been well received publicly. In order to ensure that the application of technical lessons from the disaster did not have to wait until the public inquiry was completed, he had also established an immediate technical investigation, the results of which would be made available to the public inquiry. He presently estimated that the Piper Alpha disaster would result in a production loss of about 4.2 million tonnes of oil in each of the years 1988 and 1989, together with an insignificant loss of gas production. He also estimated that the adverse effect on the balance of payments,

excluding insurance claims, would be of the order of £250 million in 1988 and £230 million in 1989, with the loss to the Exchequer being of the order of £170 million in 1988-89 and £160 million in 1989-90. He would keep these estimates under review, and see that his colleagues were kept informed. The trade unions were endeavouring to use the incident to establish a special position for themselves on safety issues in North Sea oil production with the objective of promoting union membership. Although the Department of Energy acted as the Health and Safety Commission's agent under the Health and Safety at Work Act, a number of other Departments and organisations were also involved in the safety arrangements in the North Sea, and Mr Roger Lyons, the deputy general secretary of the Manufacturing, Science and Finance Union, had acted absurdly in blaming the Department for a helicopter accident that was within the responsibility of the Civil Aviation Authority. Mr Lyons was in a singularly poor position to offer any criticism since he had been one of the members of the Burgoyne Committee on Offshore Safety who had dissented from that Committee's recommendations, which had been implemented by the present Government. Nor was the forthcoming visit by Norwegian trade unionists likely to assist the trade unions' attempts to secure a greater role in safety issues: the British public was sceptical of such aspirations by trade unions, and it was a fact that the worst North Sea accident prior to the Piper Alpha disaster had taken place in the Norwegian sector. He would continue to resist pressure from the trade unions for publication of his Department's reports on an incident on the Piper Alpha platform in 1984 and on the routine inspection of the platform that had been concluded just before the disaster, though these reports would naturally be available to the public inquiry and in fact the recommendation of the 1984 inquiry had been implemented. It was most important that the trade unions' attempts to make capital out of the disaster, and to jeopardise North Sea oil production, should be firmly opposed.

Inquiry into
an Apparent
Discovery of
Plutonium at
Drigg

THE SECRETARY OF STATE FOR ENERGY said that he would announce by way of a Written Answer later that day that he and the Secretary of State for the Environment were jointly establishing an inquiry by the Health and Safety Executive and HM Inspectorate of Pollution into the presence at Drigg low level radioactive waste disposal site of a canister apparently containing plutonium. The canister, which should certainly never have been at Drigg, had been discovered under several feet of earth, and it seemed likely that it had been there for up to 15 years.

Unemployment
Previous
Reference:
CC(88) 21.2

THE SECRETARY OF STATE FOR EMPLOYMENT said that the unemployment figures for June would be published that day. The seasonally adjusted total had fallen by 39,000 to 2.375 million. This was the 23rd consecutive monthly reduction, which was the longest continuous period of falling unemployment since the Second World War. The overall total had fallen by 86,000 in the previous month and now stood at the lowest figure for

nearly seven years. The rate of unemployment had fallen to 8.4 per cent. Unemployment had fallen by 550,000 in the 12 months since the General Election, with the largest reductions having occurred in the West Midlands, the North West and the North. Unemployment among school leavers had fallen by 32 per cent over the previous 12 months and by more than 50 per cent over the previous five years. The position on unfilled vacancies continued to be very healthy: there were 255,000 unfilled vacancies at job centres and it was estimated that there were over 700,000 vacancies in the economy as a whole.

The Cabinet -

2. Took note.

FOREIGN
AFFAIRS

Terrorist
Attack on
Greek Cruise
Ship

3. THE FOREIGN AND COMMONWEALTH SECRETARY said that the terrorist attack on the Greek cruise ship "City of Poros" on 11 July had resulted in 47 injured and 11 dead according to latest casualty figures. There were no reports of any British missing or injured. Photographs had been released of four Arabs believed to have been involved in the attack but the woman associated with them in press photographs had turned out to be a French tourist. It was also now less certain that the terrorists had escaped from the cruise ship by boat. There was speculation that the attack had been carried out by the terrorist organisation Abu Nidhal, but there was no evidence to support this. The attack would help to make the Greek Prime Minister, Dr Andreas Papandreou, realise how seriously terrorism had to be taken and might in the longer run lead to some improvement in Greek attitudes toward international co-operation.

Persian
Gulf

Previous
Reference:
CC(88) 23.3

THE FOREIGN AND COMMONWEALTH SECRETARY said that the results of the United States investigation into the accidental shooting down of an Iranian Airbus on 3 July were not yet complete. Meanwhile, the United States had agreed to pay compensation to the families of the victims. A technical investigation was also to be undertaken by the International Civil Aviation Organisation. Discussions to end the Iran/Iraq war continued in the United Nations Security Council where the United Kingdom's aim remained the need for full implementation of Security Council Resolution 598, of which the first anniversary of its adoption would be marked in a few days. It was important that the Airbus incident should not distract international attention from this objective. The Iraqis continued to obtain military success in the conflict, which made them less amenable to pressure within the United Nations.

THE SECRETARY OF STATE FOR DEFENCE said that he had paid a visit to Kuwait earlier that week where he had found great appreciation of the role being played in the Gulf by the Royal Navy. The Armilla patrol was now escorting some 80 ships in and out of the Gulf every month, which

was more than all other Western Navies put together. His interlocutors in Kuwait were convinced that the shooting down of the Airbus had been the consequence of an Iranian conspiracy. They had pointed to the fact that some of the bodies of the passengers had been recovered wearing life jackets, which argued against an attack which had taken the aircraft entirely by surprise. The Kuwaitis were also convinced that there had been an Iranian military aircraft flying in the shadow of the Iranian Airbus. The Kuwaitis perception was of increasing war weariness in Iran. Iranian prisoners of war seemed glad and relieved to be captured. There were reports of Iranian women hiding their children to avoid military conscription.

Soviet Union
Previous
Reference:
CC(88) 12.3

THE FOREIGN AND COMMONWEALTH SECRETARY said that there had been no easing of the tension between Armenia and Azerbaidjan over the status of the Nagorno-Karabakh enclave. There was no obvious way out of the dilemma confronting the Soviet leadership in Moscow. There was still no date set for the promised plenum on the nationalities question.

THE SECRETARY OF STATE FOR WALES said he had visited the Soviet Union the preceding week and had been able to see for himself the remarkable change of attitudes brought about by the way the Special Party Conference had been conducted. The impact had been particularly marked in individual republics such as Georgia where public opinion was delighted by the changes: they saw these as implying a much greater devolution of decision-taking from the centre.

Southern
Africa
Previous
Reference:
CC(88) 23.3

THE FOREIGN AND COMMONWEALTH SECRETARY said that discussions between the United States, Cuba, South Africa and Angola were continuing. The United States Assistant Secretary for African Affairs in the State Department, Mr Chester Crocker, had taken a very positive line that morning in his comments about South African agreement in principle over withdrawal from Namibia in return for Cuban troop withdrawal from Angola. There had been an indefinite postponement of the execution of six Africans convicted of complicity in murder (the Sharpville Six), to allow due legal process to be exhausted. It was too early to say whether this postponement signified a more fundamental change by the South African Government on the fate of the prisoners concerned.

Meanwhile, the Leader of the Opposition, Mr Neil Kinnock, was continuing his tour of Southern Africa. British diplomatic posts had avoided comment. Reactions in the British press had been no more than lukewarm.

The Cabinet -

Took note.

4. The Cabinet considered a memorandum by the Chancellor of the Exchequer (C(88) 10) on economic prospects and a memorandum by the Chief Secretary, Treasury (C(88) 11) on the 1988 Public Expenditure Survey.

THE CHANCELLOR OF THE EXCHEQUER said that his paper set out the prospects for the economy. In many ways performance and prospects were very good. Output, investment and employment were all growing rapidly. Confidence in the economy was high, both in this country and abroad. There was however some cause for concern over the prospects for inflation and the balance of payments. As to inflation, his current forecast (which would not be published) for a year on year increase in the Retail Price Index in the last quarter of the year of $5\frac{1}{2}$ per cent, some $1\frac{1}{2}$ per cent more than the forecast made in the Budget. Of the increase of $1\frac{1}{2}$ per cent, about half resulted from the expected increase in mortgage interest rates, and half from a rise in underlying inflation caused mainly by the monetary relaxation which all countries had felt it wise to make after the Stock Exchange crash. The rate of inflation must be brought down. Interest rates had therefore already risen and if necessary would be raised further. As to the balance of payments, he was now forecasting a current account deficit in 1988 of £9 billion. The size of the deficit need not cause alarm as long as external confidence was maintained. Government finances were in surplus. The deficit reflected private sector demand and would reduce as growth in the economy fell back to a sustainable level. Nevertheless, the deficit had to be financed and it was therefore essential to retain the confidence of the markets. This required the Government to continue to follow prudent policies, and especially to maintain firm control of public expenditure. The recommendations in the Chief Secretary's paper were crucial in this respect.

THE CHIEF SECRETARY, TREASURY said that the Government had consistently followed a policy of reducing the ratio of public expenditure to Gross Domestic Product (GDP). This policy should be continued. He had therefore proposed that the objective for this year's Survey should be that public expenditure should be held as close as possible to the existing planning totals and that, after excluding privatisation proceeds, the ratio of total public expenditure to GDP should continue to decline steadily over the next three Survey years.

Decisions had already been made which would lead to an unusually large addition to public expenditure the following year, especially the settlement on local authority expenditure and the nurses' pay award. Very substantial bids had been received in addition from Departments. They were well beyond what could be afforded and difficult decisions would need to be taken to ensure that the objective was achieved. The bids for Education, Transport and Home Office programmes were for big increases above the baseline and would need to be scaled down considerably. Most of the big Social Security bid reflected estimating changes, but policy changes to offset it would have to be considered. On Health, he would need to scrutinise in particular the bid for higher capital spending, which would have revenue consequences for later years. Difficult decisions would be needed also on the programmes for Defence, Trade and Industry, and Agriculture, and also on Employment where

account must be taken of the fall in unemployment. Among other bids, territorial expenditure would have to be scrutinised, especially in areas where spending was at a higher rate than in England. Finally, he would need to consider very carefully the bids for more spending on construction, in view of the evidence of excessive pressure on the construction industry.

Bids for increases in running costs were also very high. They implied a rise of 9 per cent in money terms and 5 per cent in real terms, and an increase in Civil Service numbers back above 600,000 within two years. He proposed repeating the previous year's objective of holding the share of running costs in planned expenditure roughly constant. This would mean a settlement well below the level of the bids, and continuing efforts to improve efficiency through effective management plans. Some of the plans produced by Departments were very good, but others required more work. Finally, as to nationalised industries, he proposed that the aim, so long as they remained within the public sector, should be to keep overall provision to baseline or less.

In discussion the following main points were made -

- a. The Government's success in managing the economy resulted from its steady pursuit of prudent policies, including effective control of public expenditure. Its reputation for sound management of the economy was a major political asset. It must continue to pursue these policies.
- b. The country's economic success had also raised its standing abroad. It was important to retain international confidence in the British economy, especially in view of the need to finance the current account deficit.
- c. The long-term consequences of expenditure decisions had to be borne in mind. Expenditure once started could be hard to stop, even if economic conditions generally changed. It would be unwise to take action now which might have to be reversed towards the end of the Parliament.
- d. The current upturn in inflation was worrying. It carried the risk of a return of inflationary expectations. The high level of pay settlements was one of the most disturbing features of the economy and had a direct influence on the size of bids. It might be however that it was a result of the very high rate of company profitability and that employers' resistance to higher pay would become stronger as profitability returned to more normal levels with a decline in the rate of growth.
- e. The high rate of increase in earnings in the economy as a whole also produced problems for public sector management. Some groups in the public sector had fallen behind the private sector, and indeed more favoured public sector groups, in their pay.

f. The high rate of pay increases in the economy generally had made the recruitment and retention of civil servants more difficult, in some cases to the detriment of the efficient running of Departments. There might indeed be a choice to be made between holding down running costs to the minimum and maintaining departmental efficiency and services to the public at the level which had come to be expected.

g. One way of containing running costs while also contributing to a more even spread of economic activity throughout the country would be further relocation of the Civil Service outside London and the South-East.

h. Decisions about expenditure on capital investment should take account of its effect on long-term economic growth, and also of its political attractions. Higher inflation and the current account deficit were the result of conditions in the private sector, not of excessive spending in the public sector.

THE PRIME MINISTER summing up the discussion, said that the Cabinet were agreed on the need for continued firm control of public spending. They endorsed all the recommendations by the Chief Secretary, Treasury. He should now, as proposed, conduct bilateral discussions with spending Ministers in the usual way against the objectives which had been agreed. She hoped that Ministers would in these discussions bear in mind the points made at this meeting, and that the bilaterals would result in agreement. If they did not, she would at the appropriate time establish a small group under the chairmanship of the Secretary of State for Energy, which would consider outstanding issues and make recommendations to the Cabinet. Ministers who were unable to reach agreement with the Chief Secretary would not be able to count on getting such good terms as a result of discussion in this group.

Meanwhile, in reply to questions she would explain that the Cabinet had held its usual July discussion of public expenditure, that they had agreed that public spending should be held as close as possible to the existing planning totals so that the share of public spending in national income should continue to decline steadily over the three Survey years, that with this objective the Chief Secretary would hold bilateral discussions in the autumn and that in the light of these the Government would take decisions on individual programmes and the planning totals, which would be announced, as usual, in the Autumn Statement in November. Other members of the Cabinet should adhere to this line in any outside contacts. The bilateral discussions should be carried on in confidence and the press should be given no ground on which to base speculative stories of Ministerial disagreement.

The Cabinet -

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

SECRET

2. Approved the proposals in C(88) 11 and invited the Chief Secretary, Treasury to proceed accordingly.
3. Noted that the Prime Minister would, if necessary, establish a small group under the chairmanship of the Secretary of State for Energy to consider outstanding issues in the autumn and make recommendations to the Cabinet.

Cabinet Office

14 July 1988

SECRET