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PRIME MINISTER

WATER PAY

We cannot of course anticipate what will be recommended by the Committee of Inquiry into the water industry pay dispute. But the amount already offered by the National Water Council gives grounds for anxiety that a high figure could be proposed. We must obviously be concerned about the risk that this could have damaging repercussions elsewhere in the public sector and more widely. In particular, negotiations are already in progress with the gas and electricity manuals, with the local authority manuals, and with the teachers; and we will soon be making an opening offer to the non-industrial Civil Service.

2. In the initial reaction to the findings of the Inquiry, it will be particularly important to focus public attention on the undiminished need for pay restraint. I attach a speaking note which colleagues could use for this purpose.

3. But we also need to take stock of the implications and consider possible action. As soon as the likely shape of a water settlement is known I suggest that officials should prepare an assessment of the settlement and its possible implications, taking account of the general economic background. The aim would be to identify any steps which could usefully be taken to minimise potential repercussions. If you agree, this would provide a basis on which colleagues concerned could meet to discuss the issues in the latter part of next week. Following the pattern of MISC(66) and MISC(80) I could chair the discussion unless you wished to do so. We may, of course, find that there are no very novel conclusions to be drawn, but I do not think we should assume that without adequate consideration.

4. I am copying this minute to members of the Cabinet, and to Sir Robert Armstrong.

(G.H.)

18 February 1983

PAY SPEAKING NOTE

1. High pay settlements are bad news for everyone. They mean fewer jobs, and higher costs and prices. They reduce the ability of commerce and industry to compete in both home and overseas markets.
2. Either employers have to find the cost of excessive increases themselves, or they must pass the cost on to others. In either case jobs, investment, and living standards are threatened.
3. The more high pay settlements we get now, the lower our living standards will be in the long run. It is therefore important that they should not be imitated.
4. That has been the history of the past decade. Earnings in Britain increased nearly fivefold. In the United States and Germany they little more than doubled. But instead of our living standard catching up with theirs, it fell further behind.
5. Wrong that lower pay settlements mean less demand in the economy and fewer jobs. As long as pay settlements are kept low, Government's economic policies will ensure sufficient money demand to provide for more jobs and output, not less.
6. Benefits of lower exchange rate for export prospects will only endure if pay settlements are kept low. Earnings growth is still in line with the average for our major competitors, and well above the level in key countries, like Germany and Japan.
7. Inflation is down to 4.9 per cent over the last 12 months. Earnings over the past year were up by nearly 8 per cent (after allowing for earnings drift as well as pay rises). Wrong to claim that

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the living standards of those in work have suffered, or that 'catching-up' is needed now. On the contrary, those in work have been enjoying rising living standards at the expense of the growing number of unemployed.

8. With inflation at 4.9 per cent, low single figure pay increases are generally the most that can be looked for. Many workers are settling for much less. Precise amounts will of course depend on individual circumstances.