PRIME MINISTER c.c. Mr. Wolfson

BNOC

David Wolfson and I have been over the figures in Annex I of Mr. Howell's paper, and it is pretty clear to us that from a purely financial point of view option (b) - selling off 75% of the shares - is much the worst of the three options considered.

Paragraph 4 of the Annex is the one to look at. This shows the benefit to - or where there are brackets, the worsening of - the PSBR if we go for option (a) or option (c) as compared with option (b). The two lines (i) and (ii) represent higher and lower capital spending by BNOC respectively. Lines (ii) reflect BNOC's latest spending plans and are therefore the more relevant.

Option (a) - i.e., status quo - is worse for the PSBR than option (b) by £140 m. in 1980/81. Thereafter, except for a tiny (£5 million) negative effect in 1982/83, option (a) is far better.

Option (c) - selling off 49% of the shares - appears to be about the same as option (a) except for rather smaller benefits in later years. In fact, the figures are misleading because they do not take account of the proceeds from selling the 49%. Strictly speaking, Mr. Howell is correct because selling shares in a company which is to remain in the public sector does not count, according to the Treasury rules, as a reduction in the PSBR. However, selling these shares would be a great help in financing the PSBR - i.e., they reduce the amount of gilts we have to sell and the markets would recognise this. If the proceeds of the 49% share sale were included in the figures in paragraph 4 of the Annex, they would be improved by nearly £600 m. over the first 2-3 years.

Taking into account the Chancellor's need for finance in 1980/81, option (c) thus looks the best.

This paper also fails - like its predecessors - to cover the point that there are increasing signs that OPEC countries prefer to do business on a government-to-government basis. BNOC (Trading), which will be 100% government owned, might be able to fulfil this role; but we know that some producers want help on the operating side in return for access to oil. This would be an argument for retaining a unified BNOC with the government holding at least a majority stake in BNOC (operating).

Finally, if the object of the privatisation exercise is to raise money, we know that there are other ways of achieving this besides selling shares in BNOC (Operating). One such method which BNOC has proposed and which has never been mentioned by D/Energy is to sell shares in BNOC's royalty oil. According to BNOC, this would raise far more money at smaller future cost to the Exchequer than selling shares in BNOC (Operating).

We think there is a strong case for asking for an inter-departmental assessment of the various sale options. Energy have been unwilling to process their paper interdepartmentally: this is why it has failed to set the facts out properly.

T.L.

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