

A

PRIME MINISTER

International Energy Targets

This issue is getting hot in the preparations for the IEA Ministerial meeting on 22nd May and for the Venice Summit.

At the IEA Ministerial on 10 December all IEA countries committed themselves to limits for their oil imports for 1980 and goals for 1985. The figures for the UK were net imports of 12 million tonnes and - 5 million tonnes respectively. IEA Ministers agreed to meet again in the first quarter of 1980 (deferred to 22 May) to consider adjustment of the 1980 limits to the extent which proved necessary on the basis of oil supply and demand developments. The Americans now seem to have acquiesced in the majority view that the 1980 ceilings should not be adjusted (unless the market gets much tighter). They are however pressing hard for national ceilings on net oil imports in 1981, a reduction in the agreed goals for 1985 and some sort of international energy targets for 1990.

Our objective at the IEA Ministerial meeting and the Venice Summit is to achieve a common reaffirmation of the hazards of the West's dependence on oil imports in 1990 on the scale suggested by current trends, so as to create the climate within each oil consuming country for effective action to reduce that dependence but without forcing upon governments the whole responsibility for that action. International oil targets as currently promoted by the USA are in danger of becoming a proxy for action. The system is however now too well established to be abandoned altogether. The Americans at the highest level are heavily committed to targets both in public and in contacts with other governments. Recent developments in Iran, emphasising the fragility of Western oil supplies, are likely to

make the Americans even more sensitive. And international targets have a part to play, but not in the form of rigid ceilings which could serve both to set a precise standard for OPEC production cuts and force us into government-run oil allocation arrangements in a supply situation less serious than that which would trigger the IEA emergency arrangements.

We should if possible resolve this issue at the IEA Ministerial leaving the Venice Summit free to concentrate on broader issues of policy. Events in the Middle East may of course bring about a completely new situation in the next few weeks. But for the moment I suggest that we should work for a compromise on the following lines (see annex for more detailed assessments):-

(a) 1981

There are at present no national targets for net oil imports in 1981. But the Community are committed by the Strasbourg meeting of the European Council to keep their total net imports within 472 million tonnes and the Community countries represented at Tokyo agreed to break this figure down on a national basis.

We should therefore agree in principle to national targets for net oil imports provided they take the form of instruments for monitoring progress towards longer term objectives but not of ceilings which cannot be exceeded. It may be desirable to leave the actual fixing of figures until later in the year. But a straight projection from our target for 1980 to that for 1985 would give us a figure of 8 million tonnes net imports. We should be able to live easily within that and could if necessary drop to a target nearer net self sufficiency.

(b) 1985

Immediately we can argue that it would be absurd to adjust medium term goals in May less than six months after they were set. We cannot accept a more rigorous goal than the -5 million

tonnes agreed in December without limiting our freedom of action on depletion policy to an extent inconsistent with the decisions of E Committee on 11th March (E(80)9th meeting Item 1). But it is difficult to argue that these goals should not be reviewed from time to time in the light of changes in both supply and demand. We should therefore indicate a readiness in principle to review the goals preferably in 1981 but if necessary at the end of this year. By then the US attitude may be very different. If it is not we would face a difficult negotiation in which we would have to argue on merits that any major increase in UK net exports would involve a wasteful use of resources of value to the IEA as a whole.

(c) 1990

We should try to confine international discussion to agreement on the long term need to restructure the world energy economy for the 1990s. This would preclude international commitment as to the means, but we might agree on a very small number of key forecasts (preferably in the form of ranges) for the IEA group of countries as a whole and also for the Community as a whole which would provide a measure of the effectiveness of the various actions being taken within each Member State, according to its circumstances, in order to transform the situation. Possible indicators are oil imports, relationship of energy to GNP, and oil as a percentage of energy use. I should prefer to avoid an oil consumption forecast as such because it would rob us of an element of flexibility at the time as between possible heavy handed measures further to reduce consumption and the alternative of stimulating additional production.

A compromise on these lines would not harm UK interests. It would be a small price to pay to avoid a major and unnecessary dispute with the Americans in the IEA. It would be likely to get wide support. At present only the Germans and Swiss are holding out against any use of

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figures and I doubt if the Germans will stand out when it comes to the crunch. The compromise would give the Americans a way out of their present extreme position if they choose to take it. They may not: but we lose nothing by trying.

I should therefore be grateful to have your agreement and that of our colleagues most concerned to our working towards a compromise on the lines set out in the paragraph above in the further preparations at official level which will start with a meeting of the IEA Governing Board on 23rd April. I shall of course consult you nearer the time and in the light of developments on the line to be taken at the IEA Ministerial itself both on targets and on policy issues likely to arise.

I am sending copies of this minute to the Foreign and Commonwealth Secretary, the Chancellor of the Exchequer and Sir Robert Armstrong.

JA.

SECRETARY OF STATE FOR ENERGY

14 APRIL 1980

INTERNATIONAL ENERGY TARGETS

1. This note examines the implication for the UK of specific target levels for 1981, 1985, and 1990.

EXISTING TARGETS FOR 1980-85

2. (i) European Council, Strasbourg, June 1979: resolved to maintain Community net oil imports between 1980 and 1985 at an annual level not higher than that for 1978 (ie. 472 m tonnes).

(ii) Economic Summit, Tokyo, June 1979: participants agreed national oil import ceilings for 1985. France, Germany, Italy and the UK expressed their will to take as goals for a ceiling on oil imports in 1985, the 1978 figure (Italy in the context of the overall Community commitment). They undertook to recommend to their Community partners that each Member country's contribution should be specified the Community's annual goal for 1980 to 1985 of 472 m tonnes net oil imports.

(iii) Summit Energy Ministers, September 1979: in the run-up individual EEC net oil import targets for 1985 were agreed. The UK accepted - 5 m tonnes, and made clear that should UK net exports exceed 5 m tonnes, this would be entirely a matter for the UK and would not affect other Member States' targets.

(iv) EEC Energy Council, December 1979: agreed national net oil import targets for 1980, the UK accepting 12 m tonnes.

(v) IEA Ministerial, December 1979: agreed national net oil import limits for 1980 and goals for 1985 for all members, within the IEA's group target of 24.5 mbpd (1980) and its goal of 26.2 mbpd (1985). The national targets for each country are indicated in ANNEX A attached. The UK's targets were confirmed as 12 m tonnes (1980) and - 5 m tonnes (1985).

INTERNATIONAL OIL OUTLOOK

3. Any assessment of the outlook is subject to major uncertainties. It is too early to reassess how valid present targets will be in relation to expected supply and demand, and moreover the international supply outlook may change in the next few months. Our best estimate, however, is that, since acceptable levels of economic growth may take some time to re-establish, the supply/demand position in 1985 is likely to be broadly in balance. The downside risks, however may be the greater. The difficulties of arriving at firm estimates are, of course, much greater for 1990.

4. Apart from the unforeseeable political risks (eg renewed unrest in Iran) there are major uncertainties on both the supply and demand sides of the equation. Production levels in many OPEC countries will be influenced by governments' assessments of optimum depletion rates, foreign exchange requirements, and possibly also by "extraneous" factors, such as the climate of political relations with the West. We do not expect OPEC production to rise significantly above its present level in the next decade. The demand for OPEC oil is a residual, after other sources of oil have been deducted from total oil demand, thus sensitive to quite small changes in the key variables - particularly economic growth rates, effects of price changes on consumption, relative prices of alternatives and the scope for substitution.

5. The following table summarizes our current provisional view of prospects between now and 1990 (see also Annex B).

OIL DEMAND AND SUPPLY mmbd

	1981	1985	1990
A. DEMAND			
IEA	36.2	38-39	39-42
Rest of Non-Communist World	14.5	15.3-16.3	16.4-20.4

B. SUPPLY (exc
OPEC oil)

	1981	1985	1990
IEA	15.3	15.8	15.8
Rest of Non- Communist World	36.1	40.5	41.6
: of which OPEC	28.7	32.0	32.0
Surplus/(Deficit) of OPEC oil	0.7	1.0-3.0	2.0-(5.0)

6. Our assessment assumes that the real oil price rises at 2% pa from 1980 to 1990, and that the OECD economic growth rate lies within the range 2-3% pa. Given our assumption of future OPEC production (32 mmbd) there could be excess capacity in 1985 and possibly in 1990. However, our assessment depends critically on the OPEC production assumption chosen: the Americans believe OPEC production could be much less (in the range of 21-30 mmbd in 1990). Clearly a much lower production figure for OPEC could turn a projected surplus into a deficit. The IEA Secretariat also takes a pessimistic view: a deficit of 3.9 mmbd in 1985, and of 8.7 mmbd in 1990. (Their results are the product of higher economic growth assumption than our own, together with a higher projection of non-IEA oil consumption, and less replacement of oil by other energy forms).

1981

7. The latest forecasts of the UK position for 1981 are:-

Oil production 85 - 105 million tonnes

Oil consumption 85 - 95 million tonnes

The oil production range takes account of some downside risk, and use of depletion control. The upper end of the consumption range assumes a trend growth of GDP of 2% pa from 1978 onwards. The lower end is consistent with the post-Budget forecast published in the PSBR, followed

by zero growth till the end of 1981.

8. These forecasts give a range for net imports from + 10 to - 20 million tonnes. In considering a target however it would be imprudent after allowing for downside risks and (some) depletion measures to count on production of more than 90 million tonnes. If targets are to be used mainly as a means of monitoring progress against medium and long term objectives the consumption estimates used should take account of long term trends as well as short term prospects. This suggests a figure at the top end of the range shown. Thus a reasonable target for 1981 would be net imports of 5 million tonnes (compared with a target of 12 million tonnes and a likely outturn of 7 - 9 million tonnes in 1980). But we could, under pressure, move closer to a figure of net self-sufficiency provided that it was clearly understood by our partners that there would then be no room for improvement in the immediately succeeding years. However the more rigidly the target is defined the less we can move.

1985

9. As para 5 above shows our view of the international outlook for 1985 is that supply and demand is likely to be roughly in balance. We are committed to a goal of net exports of 5 million tonnes. As the following table shows any revised goal which implied higher net exports would limit our freedom of action to implement depletion policy:-

	M tonnes
Oil production (assuming maximum depletion measures and no further slippage in development and production)	90 to 100
Oil consumption (assuming economic growth of approx 1-2½% for 1979-85)	90 to 100

1990

10. The latest IEA forecasts estimate oil consumption in 1990 at 42.8 mbpd compared with 37 mbpd in 1980. This involves net imports of 28 mbpd in 1990 compared with an expected 22 mbpd in 1980.

11. Targets also need to take into account the likely availability of OPEC oil. The present IEA view is that the OPEC oil available to OECD countries in 1990 will be as little as 19.3 mbpd. (In our view, the IEA projections for oil consumption by non-IEA OECD countries, non-OPEC LDCs and net Communist Imports are rather high).

12. Targets should be sufficiently rigorous to act as an incentive to Governments to implement the long-term policies on which we are all agreed. Against that requirement, and the general picture described in paras 3, 6, 10 and 11 above, group targets for 1990 might be:-

	<u>mbpd</u>
Consumption	28 to 40
Net Imports	22 to 25

13. The latest proposals from the IEA are for a target of 22-24 mbpd. We could, therefore, broadly accept this approach since it coincides fairly closely with our own judgement.

14. Two other approaches to targets are:-

a) Oil as a percentage of TPE

In 1980, for the IEA group as a whole, oil will provide 51% of TPE. The IEA percentage should decrease because of growing use of other energy forms and, for 1990, a reasonable group target might be about 45%. This should give no trouble to us since we are likely to be below 45% anyway, but we might come under pressure to do even better in order to help the IEA as a whole.

b) Energy Elasticity

This is the percentage change in total primary energy use



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divided by the percentage change in GDP which for the years 1978-85 is expected to average 0.7. But it is unsatisfactory as an indicator partly because, for the period in which 1990 falls, it is thought unlikely to drop much further below 0.7, and partly because, on its own, it says nothing about oil consumption and must, therefore, be read in conjunction with the "oil as a percentage of TPE" indication.

Department of Energy
15th April 1980

All IEA countries firmly committed themselves to limit their oil imports in 1980, and to pursue goals for their oil imports in 1985.

COUNTRY

	1980		1985	
	MTOE	MBDOE	MTOE	MBDOE
Australia	13.5		17.0	
Austria	11.5		13.5	
Belgium	30.0		31.0	
Canada	7.4	0.15	29.4	0.6
Denmark	16.5		11.0	
Germany	143.0		141.0	
Greece	14.8		16.5	
Ireland	6.5		8.0	
Italy	103.5		124.0	
Japan	265.3	5.4	308.66	6.3
Luxembourg	1.5		2.0	
Netherlands	42.0		49.0	
New Zealand	4.2		4.4	
Norway	-15.5		-18.3	
Spain	51.0		52.9	
Sweden	29.9		29.0	
Switzerland	14.0		14.5	
Turkey	17.0		25.0	
United Kingdom	12.0		-5.0	
United States and Territories	437.2	8.9	436.0	8.9
IEA total	1,205.3	24.5	1,289.56	26.2
less bunkers		1.4		1.6
		<u>23.1</u>		<u>24.6</u>

Table 1

ENERGY DEMAND AND SUPPLY: mmbd

	1978	1981	1985	1990
<u>Demand</u>				
OECD	74	75	82-84	88-97
IEA	69	69	75-77	81-89
Non-OECD	17	19	21-22	25-30
TOTAL	92	94	103-106	113-127
<u>Supply (exc OPEC oil)</u>				
OECD	47	52	57-59	63-68
IEA	45	49	54-55	59-64
Non-OECD	13	15	16-17	20-24
TOTAL	61	66	73-76	83-92
Demand for				
OPEC oil	31	28	30	30-35
Willing OPEC				
production	30.3	28.7	32.0	32.0

TABLE 2

IEA DEMAND ON OPEC OIL

IEA FIGURES	1985	1990	OURS	1985	1990
IEA OIL PRODUCTION	14.8	14.8		15.8	15.8
IEA OIL CONSUMPTION	41.1	42.8		38-39	39-42
Net Oil Imports	26.3	28.0		22.2- 23.2	23.2- 26.2

Note: Totals do not sum because of rounding.



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10-10	10-10	10-10	10-10
11-11	11-11	11-11	11-11
12-12	12-12	12-12	12-12
13-13	13-13	13-13	13-13
14-14	14-14	14-14	14-14
15-15	15-15	15-15	15-15
16-16	16-16	16-16	16-16
17-17	17-17	17-17	17-17
18-18	18-18	18-18	18-18
19-19	19-19	19-19	19-19
20-20	20-20	20-20	20-20
21-21	21-21	21-21	21-21
22-22	22-22	22-22	22-22
23-23	23-23	23-23	23-23
24-24	24-24	24-24	24-24
25-25	25-25	25-25	25-25
26-26	26-26	26-26	26-26
27-27	27-27	27-27	27-27
28-28	28-28	28-28	28-28
29-29	29-29	29-29	29-29
30-30	30-30	30-30	30-30

UNITED STATES DEPARTMENT OF STATE
 OFFICE OF THE ASSISTANT SECRETARY FOR
 PUBLIC AFFAIRS

Washington, D.C. 20520

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 HAS RECEIVED FROM THE
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 THE ECONOMIC
 DEVELOPMENT OF
 THE MIDDLE EAST
 DATED APRIL 15, 1980

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