

PRIME MINISTER

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PRICE OF OIL AND THE BUDGET

plus 23/2

1. Since a reduction in the price of oil is exactly analogous to a reduction in an excise tax, we ought to consider prospective oil price decreases as part and parcel of the process of fixing tax rates for next year. The Chancellor will be telling you that the BNOG believe that the average price of North Sea Oil in 1982/83 will be \$32 per barrel, about \$3.50 less than the price in the first quarter of 1982. This will give rise to a reduction of about £650m in North Sea revenues in 1982/83 and £1½bn in 1983/84. The PSBR effect would be somewhat less than this, depending upon the devaluation of sterling against the dollar. But if you accept the oil price forecast, it would in my view be unwise to plan for less than a £½bn shortfall of revenue in 1982/83.
2. I think I ought to make my own view known, however. I believe that the fall in prices will be even greater than the BNOG's commercial judgement suggests. You will recall that in the predictions of the Department of Energy, such as those which appeared in the Electrification Report, the Department always showed a price of oil which was increasing at unbelievably high rates. These forecasts seem to me to deny the inexorable laws of demand as firms invested more and more in processes which were energy-saving.
3. I believe we ought to consider seriously the possibility of a fall well below \$30 in 1982/83. We have been caught before by rises in oil prices far above anyone's expectation. I suspect that we are about to witness a fall in prices which again will be sharper than anyone expected.
4. I was confirmed in this view when I discussed the issue with Walter Salomon. He said he also thought there would be a sharp fall in the price of oil which would not be reversed. I believe that the judgement of such a shrewd man as Walter Salomon should command respect; it certainly commands mine.
5. In its essence, this means that we should think in terms of at least £½bn and perhaps £1bn tax relief in 1982/83 being afforded /by this

by this shortfall in the price of oil. This strongly suggests that we should incline towards other tax reductions nearer to £1bn rather than £1½bn.

23 February 1982

A handwritten signature in dark ink, consisting of the letters 'A' and 'W' in a stylized, cursive script. The signature is positioned above a horizontal line.

ALAN WALTERS