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 Chancellor of the Exchequer
 Treasury Chambers
 Parliament Street
 LONDON
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13 March 1985

FSBR

Nigel
 Financial Statement & Budget Report (ie Red book)

I have seen the paragraphs which it is proposed should be included in the FSBR dealing with oil and coal matters. There are two aspects of these forecasts which need to be handled with great care: oil price movements and oil production.

Clearly we do not wish at the present time to signal to the market or to OPEC that we expect to see an early fall in oil prices; similarly we need to play down the fact that our forecasts of production in 1985 are higher than previously.

I am particularly concerned about the references in the draft text to oil price movements. I would prefer there to be no reference to the possibility of a fall whether in sterling, dollar or SDR terms. Can I suggest that after the third sentence of the paragraph headed "Revenue" in part 2 the text should read:

"Projections of Government revenues assume that revenue from the North Sea falls in both real and nominal terms after 1985/6 as North Sea oil output falls, or becomes less profitable, but that this is more than offset by rising revenues from the growing non-North Sea economy".

I appreciate that the forecasts do in fact assume a fall in sterling oil prices but in dealing with any questions which might follow the Budget I think we should be as evasive about this as I understand we usually are about forecasts of the sterling/dollar exchange rate. It seems to me that making public forecasts of the oil price now entail for us very similar market risks to making "official" forecasts of the exchange rate.

Today's announcement about BNOG is another reason for avoiding oil price forecasts in connection with the Budget. We do not want to multiply risks with OPEC or the market.

If you can accept the change I propose, then I hope your officials and mine can agree the wording in any press notice and briefing to reflect this point. Similarly I hope that you will clear with me

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whatever you propose to include in your Budget speech on this matter and on the sensitive topic of the cost of the coal strike.

I am enclosing with this letter a note by my officials suggesting some drafting changes and points which need clarification.

I am copying this to the Prime Minister and Geoffrey Howe.

A handwritten signature in dark ink, appearing to be 'P. Walker', written in a cursive style. The signature is located in the center-right of the page.

PETER WALKER

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FSBR - DEPARTMENT OF ENERGY POINTS

Oil

i) We note that the Treasury's central forecast for 1985/6 production is the same as the Department's but that Treasury are basing calculations for the 3 subsequent years on output 3m tonnes per annum higher than our forecast.

ii) In the proposed text itself in paragraph 3.05 redraft the third sentence as follows:

"With oil production at or near its peak and with high sterling oil prices, the production....."

iii) In the last sentence of 3.05 we think 6% is too low. The figure is more like 6½% based on BGC contract prices for gas and in round terms is probably better put at 7%.

iv) In paragraph 3.10, first sentence, delete the words "and early 1985" as prices are as much as \$2 above the 31 December levels. In the third sentence insert after the word "falling" "in 1984".

v) Re-draft paragraph 3.24 as

"North sea oil production could well peak in 1985 and with the end of the coal strike fuel imports should fall in 1985 compared with 1984. 1985 could be the peak year for contribution of oil to the balance of payments".

Coal

vi) Although we think the figures for the cost of the strike are of the right order of magnitude we will need for our own purposes to know their make-up. Could we have the detailed calculations? Subject to seeing those we are content with the text on this point.

vii) The reference in 3.39 to a reduction of about two-thirds in coal output for 1984 is put at 51m tonnes which is 44% of forecast. We suggest the reference is to output being reduced by "well over half".

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