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Energy SCW

CC: LG
Energy.

10 DOWNING STREET

THE PRIME MINISTER

22 March 1982

Dear Mr. Wilson

Thank you for your letter of 25 February on the question of world oil prices.

Your letter assumes that a fall in world oil prices will be damaging to the UK economy and that we share an interest with other oil producers in trying to maintain prices by cutting production and exports. My own view, on the contrary, is that the Western Industrial countries - and indeed the non-oil developing countries as well - will all benefit from lower oil prices through the consequent reduction in inflation and increase in real incomes. The favourable effects on the UK of these factors seems likely well to outweigh any direct loss of national income through a reduction in the value of UK net oil exports.

An agreement among all oil producers to reduce production by an equal proportion would certainly be against the UK's interests, since the effect on export volume would more than cancel out the benefit of higher prices (a 10% reduction in production would imply something like a halving of UK net oil exports); the benefits would all accrue to those few countries whose production is several times their domestic consumption. A reduction in all oil producers' net exports by an equal proportion would not be open to the same objection (although, in my view, such a cartel operation would be objectionable on general grounds); but, in any event, the UK share of world net oil exports is so small as to make our participation in such an arrangement practically irrelevant; the problem is essentially one for OPEC to tackle.

Yours sincerely

Margaret Thatcher

Gordon Wilson, Esq., M.P.

B/F annex Energy

MCS

cc Mr Walters

Content with draft reply?

MAP 16/3.

SECRETARY OF STATE FOR ENERGY

THAMES HOUSE SOUTH
MILLBANK LONDON SW1P 4QJ
01 211 6402

MAP

Yes: I have taken account of Alan Walters' points.

Mike Pattison Esq
10 Downing Street
London
SW1

16 March 1982

MLS 17/3

Type as amended for PM pl cc I.G.

MAP

Dear Mike,

Thank you for your letter of 26 February enclosing a letter from Mr Gordon Wilson MP to the Prime Minister. Mr Wilson asked my Secretary of State a closely related question in the House on 8 March (attached).

I attach a self-explanatory draft reply.

Yours ever,

JULIAN WEST
Private Secretary

DRAFT LETTER TO MR GORDON WILSON MP

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Mr. Merlyn Rees: Will the Minister confirm that gas prices have increased by 100 per cent because of the Government's actions and that the standing charge has increased by 300 per cent? As there has been a decision to increase the charge, why can there not be a decision to change it in other ways?

Mr. Mellor: Removing the differential charge for the first 52 therms of gas meant that when the Labour Government left office the standing charge was £6·37 a quarter, so the effect is not markedly different.

Oil Sales

3. **Mr. Greville Janner** asked the Secretary of State for Energy, further to his reply to the hon. Member for Southend, East (Mr. Taylor) on 8 February, *Official Report*, column 250, how much oil was exported to Israel in the most recent period for which figures are available.

The Minister of State, Department of Energy (Mr. Hamish Gray): None, Sir.

Mr. Janner: Will the Minister reconsider the unhappy policy of discrimination that has led to that sad answer? In the interests of free trade, should we not nowsell our oil to a democratic customer anxious to buy it?

Mr. Gray: The policy is not aimed against any country but is in favour of European Community and International Energy Agency countries with whom we have a special energy relationship. We should ask licencees to recognise those relationships. There are many other friendly countries to whom we do not export oil because they are not members of those alliances.

Mr. Marlow: As the Israeli war machine is the greatest threat to Middle East stability, would it not be a little absurd for Her Majesty's Government to provide it with fuel with which it could threaten world peace?

Mr. Gray: My hon. Friend's point hardly relates directly to the question.

British National Oil Corporation

4. **Dr. J. Dickson Mabon** asked the Secretary of State for Energy how many barrels of oil produced daily from the oilfields in the United Kingdom sector of the continental shelf the British National Oil Corporation handles as a trader.

The Secretary of State for Energy (Mr. Nigel Lawson): In 1981 it was 1,037,000 barrels per day.

Dr. Mabon: As that is such a profoundly overwhelming proportion of the total, does it not suggest that BNOC should remain an integrated trading, explotation and production company?

Mr. Lawson: I fail to see the logic of the right hon. Gentleman's question. The figure points to the strength that BNOC, after the flotation of Britoil, will have in the world's oil markets.

Mr. Gordon Wilson: Does the Secretary of State not recognise that the drop in world oil prices will affect the trading arm of BNOC, as it will the Government directly? Is it not time for the Government to act in concert with OPEC to cut production to maintain the price level and to save in Scotland jobs that will be lost if North Sea development does not take place?

Mr. Lawson: The fall in oil prices will have a much more positive effect on jobs in the Western world, including the United Kingdom and Scotland, than the policy that the hon. Gentleman would like us to pursue.

Mr. Archie Hamilton: Does the question asked by the right hon. Member for Greenock and Port Glasgow (Dr. Mabon) not demonstrate the fact that the SDP has great difficulty in making up its mind whether it is for or against nationalisation?

Mr. Lawson: My hon. Friend is absolutely right. The SDP has great difficulty in deciding where it stands on everything and anything.

Mr. Rowlands: Is the Secretary of State aware that BNOC is facing its greatest crisis since it was created and that the fall in oil prices has created a major problem for the trading arm, which could lose large sums of money? Does he agree that now is not the time to smash up the corporation, as it would destroy the morale of the State trading arm personnel? Will the right hon. Gentleman at least consider postponing that part of the Oil and Gas (Enterprise) Bill for at least 12 months to give the corporation a chance to weather the storm?

Mr. Lawson: No, Sir. I am confident that BNOC will remain fully capable of dealing with world economic developments and developments in the oil market as they occur.

Space Policy

Mr. Michael Marshall asked the Secretary of State for Energy with what aspects of Her Majesty's Government's space policy his Department is currently concerned.

The Under-Secretary of State for Energy (Mr. John Moore): Clearly I am concerned to ensure that my Department is aware of developments in space technology that are of interest to energy related issues.

Mr. Marshall: With the growing increase of loading for commercial satellite projects in this country and the scientific satellite development through the European Space Agency, in which Britain plays a leading part, does my hon. Friend agree that the time is now overdue for us to take a wider look at those issues? Will he carefully consider the opportunities in the remote sensing programme and for solar energy through space developments.

Mr. Moore: Knowing my hon. Friend's extensive knowledge and experience, I shall maintain my Department's watching brief.

Diesel Fuel

6. **Dr. Mawhinney** asked the Secretary of State for Energy how much diesel fuel was produced in the United Kingdom in the last year for which figures are available.

Mr. Gray: My Department's estimate is 5·5 million tonnes in 1981.

Dr. Mawhinney: Does my hon. Friend agree that the diesel engine industry is a strategic industry and that firms like Perkins in my constituency should not be exposed to unfair competition, from whatever source?

GORDON WILSON MP

Price Oil depletion

CONFIDENTIAL

3 March 1982

ALAN WALTERS

Mr Pattison

PRIME MINISTER

await D/En draft. due 12/3

Tosee

PROPOSALS BY GORDON WILSON FOR BRITIAN TO JOIN OPEC, LETTER OF 25 FEBRUARY

MAP (I have shown PM) MCS 3/3

1. I agree with Mr. Wilson's judgement that the world price of oil is likely to collapse to between \$25 and \$28 per barrel. The remainder of his letter, however, contains muddled arguments, logical fallacies, and statements which are clearly discredited by the evidence of the last ten years. However, I will only deal with the main points in this note.

2. His first statement is that the decline in oil prices will lead to freezing of oil development pending stabilisation of the market. But what determines investment and development is the prospect of after-tax profit for the oil companies. This will be calculated over the amortisation period of the assets, probably ten years or so for the average oil investment. The oil companies will take into account their estimate of the pattern of oil prices which they expect over the next ten years. Reductions in the price of oil which are seen to be transitory will have no discernible effect on investment. Furthermore, if the oil price were artificially held up by some restriction of output, then it would be known that later there would be an increase in the supply of oil which would bring the price down below the level which would otherwise have ruled. Furthermore, restrictions on output brought about by some depletion policy would necessarily reduce the overall profit of the oil companies and so give rise to lower investment, ceteris paribus. In short, Mr. Wilson's policy would be fairly certain to lower investment and development in the North Sea.

3. Mr. Wilson believes that we should make common cause with OPEC and agree to cut production in order to stabilise prices. He admits the North Sea output is a mere drop in the bucket, but somehow feels that if we agree to cut production, all other important producers will agree to cut also. The evidence of the past few years, however, is that even the Saudis, under the most auspicious circumstances, with their enormous market power have failed to control the Cartel. The high price of OPEC oil has induced a vast expansion of non-OPEC production, and given rise to the existing cuts in prices. Moreover, anything the West do in order to curtail the production of oil will simply open the gates for other producers to fill the production gap.

CONFIDENTIAL

/These countries

These countries are not merely developing countries such as Indonesia and Nigeria, anxious to pay for their development programmes, but also countries of the Eastern bloc.

4. In short, there is no way in which we could conceivably support the price of oil. But even if we could, we should not do so. Cheaper oil will give rise to widespread benefits in the Western industrialised countries which can only be favourable to Britain as well. These benefits will far outweigh the small loss in our small net export balance of oil.

5. Mr. Wilson suggests that we have a "realistic depletion policy" for oil. I think our policy should be to have a <u>profitable</u> depletion policy for oil. This will be achieved if we allow the private sector to recover oil at a rate which maximises their own profits and our revenue over the years. Mr. Wilson might reflect that if we had introduced depletion policy when we came into office, we would have reduced the production of oil during the years 1979-81 and so foregone the very large benefits which flowed from the extraordinarily high price of oil during that period. This would have been an inexcusable waste of the most valuable national asset. In 1979/80 we should have been importing expensive foreign oil in order to keep our own oil in the ground. Mr. Wilson believes that we can outguess the market. I doubt it. Governments have been singularly inept when they have played the markets. There is no reason to believe that we could do any better.

AW

<u>3 March 1982</u>

<u>ALAN WALTERS</u>

FILE

ds

Alan Walters

To see & return pl.

MLS 3/3

12/3

10 DOWNING STREET

From the Private Secretary

26 February 1982

I enclose a copy of a letter to the Prime Minister from Mr. Gordon Wilson M.P., about Government action on the crude oil price. I should be grateful for a draft reply for the Prime Minister's signature by 12 March.

I am sending copies of this letter to John Holmes (Foreign and Commonwealth Office), Jill Rutter (HM Treasury), Muir Russell (Scottish Office) and David Wright (Cabinet Office).

M. A. PATTISON

Julian West, Esq.,
Department of Energy.

ds

26 February 1982

I am writing on behalf of the Prime Minister to thank you for your letter of 25 February. I will place it before her and a reply will be sent to you as soon as possible.

M A PATTISON

Gordon Wilson, Esq., M.P.

2

10 DOWNING STREET

PRIME MINISTER

Gordon Wilson writes arguing that the Government must make common cause with other oil producing countries to stabilise the market. He has copied his letter to OPEC Governments. We will let you have a draft reply.

MAP

26 February 1982

Please show this letter to the Chancellor and the Energy Secretary; Also - should [illegible] Alan Walters advise me

cc John Gow
Press Office

Gordon Wilson M.P.

HOUSE OF COMMONS
LONDON SWIA OAA

25th February 1982

The Prime Minister
The Rt. Hon. Margaret Thatcher M.P.,
10, Downing St.,
Whitehall
London SW1A

R26

Dear Prime Minister,

Unless speedy action is taken, the world price of oil is in danger of collapse to between $25 and $28 per barrel. Already, the slide in oil prices has placed in jeopardy the chances of even a moderate reflation of the economy. Not only is it the case that oil taxation revenue will drop sharply but the decline in oil prices will also lead to the freezing of oil development pending stabilisation of the market. This will have drastic consequences for offshore and onshore oil related oil employment in Scotland.

The Government cannot duck this issue. The international oil market is spiralling downwards and, while this may impact beneficially on the Western world for a short time, it will lead inevitably to diminishing exploration and development. Such actions are vital if new reserves of petroleum and gas are to be found and won to avoid future shortages.

For Scotland there is not the same urgency over revenue. An oil tax return of £5 to £6 billion is more than adequate in a Scottish context. However, the budgetary prospects for the UK as a whole are more damaging and it serves neither Scotland nor the UK to be caught up in a low-price regime.
Oil from the North Sea is high-cost oil and it is obvious that internationally cheap oil, induced by over-production, will not be to our advantage. Indeed, the over-production of crude oil from the North Sea and Mexico has partly led to the glut and to the fiscal embarrassments now facing the UK and other oil producers.

This being so, the Government must make common cause with the other oil producing countries to stabilise the market and the price regime even if, in the interests of Western economies as a whole, it would not wish to participate in a "hike" of oil prices beyond the limits previously fixed.
The Saudi production cuts will not, of themselves, halt the slide. I understand that OPEC will probably call an emergency meeting shortly to discuss production cuts by oil producers. I hope you will request an invitation from OPEC to send an official observer and be prepared, on hearing the report, to consider, along with the oil companies who are also suffering financially from the price collapse, agreeing to cut production.

NO

Any cuts the UK may make in the North Sea will be minimal in world terms but collectively, taken with reductions made by the OPEC countries, they will have an impact.

Stabilisation of the world price for oil will restore confidence, halt the decline in oil revenues and maintain oil exploration and development. It should be made clear that the cuts in production are temporary to cope with the emergency. In the medium and longer term there is a need for a realistic oil depletion policy which will be more sophisticated and which will relate to policy over development as well as production.

This matter is of concern to all oil producing countries and therefore I am copying this letter to all members of OPEC.

Yours sincerely,

Gordon Wilson

GORDON WILSON M.P.