PRIME MINISTER

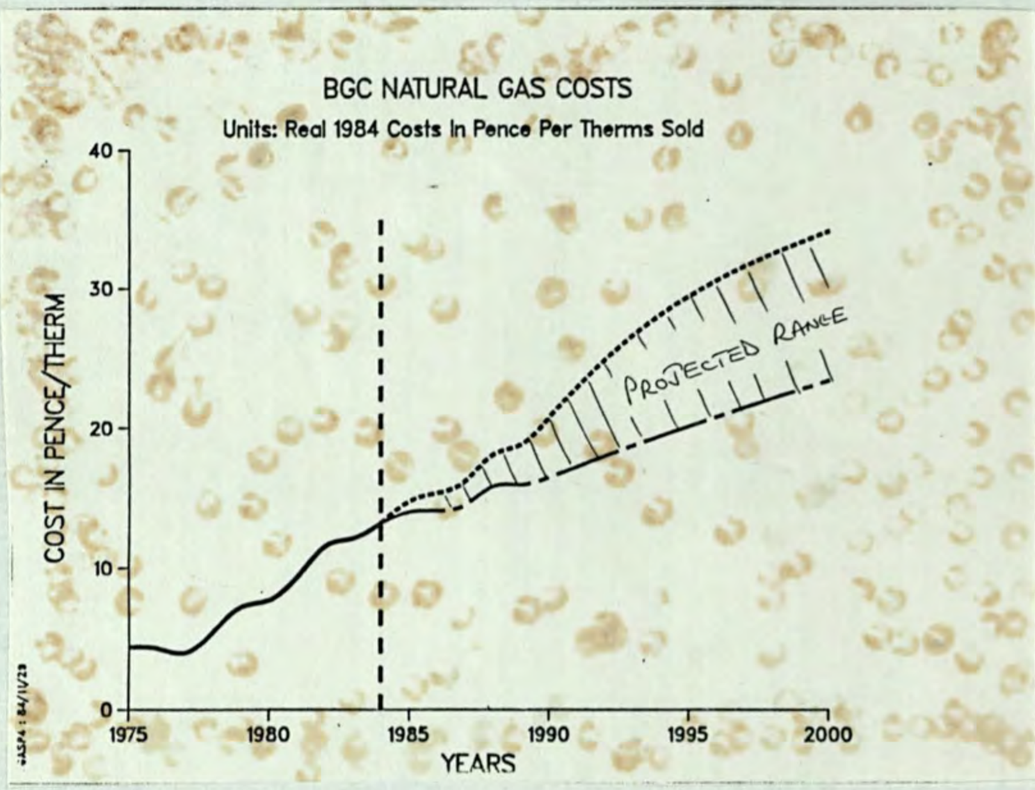
22 March 1985

BGC PRIVATISATION

If we are to accomplish the privatisation of BGC at all in the remainder of this Parliament, it will have to be with the active support of BGC and the Department of Energy. That means privatising BGC as a whole, within a framework of regulation and limited competition - from electricity, oil, and perhaps from gas producers directly supplying large customers, under the Oil and Gas Enterprise Act.

It is a pity that lack of zeal in the Department of Energy has now foreclosed more radical options to move closer to a free gas market in the UK. Nonetheless, we still have the big prize of another BT-scale step towards a property-owning democracy - and with it a further scaling down of the public sector. Moreover, the commercial disciplines on BGC, even in the form of a privatised monopoly, could be surprisingly tough; so much so, that BGC will certainly have to become more efficient and may be forced to shed peripheral activities.

This stems from the fact that the real cost of supplying gas from the North Sea is on a well-established upward trend.



BGC is currently paying an average of 13-14p per therm for gas supplies. Yet new contracts for UKCS gas are being concluded at around 25p per therm (1985 money) because the fields are smaller, less productive and require proportionately more investment than the large, low-cost fields initially developed in the southern North Sea. There is little sign of that trend being reversed. Ten years ago, gas supplies accounted for 20% of BGC's total costs. Now that figure is 40%, and rising steadily.

What does this imply for a privatised BT-style BGC? As with BT, the Government will need to have a tight grip on gas pricing to the consumer so as to prevent BGC abusing its monopoly position. But, unlike BT, which has new technology working in its favour, BGC's future margins will be squeezed between the increasing unit cost of gas supplies and tightly-regulated consumer pricing. That could really force BGC to make a hard-headed appraisal of their business objectives. They would have to concentrate their resources on core activities. They would have to face up to the disposal of peripheral assets and activities - retail outlets, land, contract services, wide-blue-yonder research, and even their upstream interests.

Conclusion

The bird in the hand may yet give us most of the benefits we have been seeking from the privatisation of BGC. We can, and should, press ahead to launch a privatised BGC early in 1987. That means:

- rapidly laying down a master timetable and adhering tightly to it;

- quickly resolving important policy questions such as how best to construct a framework of regulation to protect consumers, whether to curb BGC from expanding beyond its core activities, and whether in conjunction with privatisation to introduce a gas export regime.

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