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Prime Minister
You might like to have a word with the Secretary of State for Energy and the Chancellor at your meeting tomorrow morning.
FERB 25.3.

PRIME MINISTER

On Friday afternoon, at his request, Shaikh Yamani flew in to Yorkshire to have a talk with me on the current oil situation.

He endeavoured to give the impression that he and others in OPEC had some doubts about our BNOC announcement, and he was very concerned as to how we were going to fix the oil price for the purposes of taxation.

I strongly pointed out to him that you and I had had the courtesy to discuss our ideas on BNOC with him; that he had been strongly in favour of such action; and that it was only after such consultation that we had made our final decision. Therefore I hoped he would have appreciated that, once again, we had done everything sensible and practical to help maintain stability.

On the question of fixing prices for taxation purposes I said there would be no difficulty in doing this, and that it would not be done by means of regular public pronouncements. Indeed, there had always been variations in the prices that had been agreed for these purposes.

He suggested that we should engineer some way of fixing taxation prices above current spot market prices - which would mean higher taxation for us, and more stability for the market. I explained there was no possibility of this.

His main purpose, however, was to argue strongly that it was essential when the market was weak that HMG should use its powers over royalty oil to reduce the supply to the market. Specifically, he suggested that we could inform North Sea licensees that we would defer taking our royalty oil until a later date. He argued that this would have no adverse affect upon the companies, but would reduce the volume of North Sea production for that particular period.

I pointed out that if we acted on his suggestion there would be nothing to prevent oil companies from maintaining production at current levels and selling to the market the oil we had decided to forgo. Obviously if this happened we would not succeed in reducing the supply of oil to the market. He expressed the view that ways could be found with the oil companies for the purpose to be achieved.

He informed me that he was deeply concerned because OPEC countries were becoming very tired of maintaining their restraint on supply. He said there was now a danger that the Soviet Union would return to their normal levels of supply, having gone through a period of production difficulties. (The previous day he had had detailed talks with the Soviet representatives which led him to this conclusion).

He therefore saw a danger that the whole international pricing system might break down, unless Norway and Britain agreed to show some restraint.

He pointed out that every year the supply from the North Sea had been greater than HMG had originally anticipated, and that this year's figures were reaching alarming heights. He argued that he could not see how the United Kingdom could be other than seriously damaged if there was a substantial collapse of the oil price. He felt that unless we made some contribution to stability there would be a breakdown in the OPEC system, probably led by Nigeria, which would be directly to our disadvantage.

He asked me to convey very strongly to you that, in a world where oil demand is static, and perhaps actually reducing, one could not continue for much longer with a system whereby one section of the world restrained production, whilst other sections were actually increasing production to the maximimum. He felt that if HMG genuinely believed that oil stability was an important factor for both Britain and the western world at large we would, in the coming twelve months, have to make some positive contribution to that objective.

I explained to him the problems of putting production restraint on the North Sea and told him I would convey his views to my Government colleagues. He expressed his gratitude for that, but said that there would be nothing that would put a restraint on the North Sea more effectively than a total collapse of the world oil price.

My Department has also been alerted to this background by certain of the international oil companies who have had recent contacts with Yamani.

I attach a brief note of some of the possibilities which could be examined, if you thought it appropriate.

I am copying this minute to the Foreign Secretary and Chancellor of the Exchequer.

Peter Walker

SECRETARY OF STATE FOR ENERGY

25 March 1985

Last Summer Shell informally raised a number of ideas for cutting UKCS production at the margin, all of which would have cost HMG money, but not Shell, namely:

(a) HMG should leave its royalty oil in the ground for a number of months provided companies agreed to make an equivalent cutback in production. HMG would recover its oil as a result of higher production at some time in the future. This would be technically possible in Shell's main fields, but not in most other fields;

(b) HMG's Royalty oil should be produced, but then stored for a period;

(c) BNOC should not lift all its participation oil.

Shell was particularly keen on (a) above and almost certainly discussed the idea with Sheikh Yamani. Their partners, Esso, were strongly opposed.

In addition Shell, BP and Texaco advanced their annual maintenance programmes which temporarily reduced production. It should be possible to persuade them to do this again this year.