Prime Minister

AT 7/6

MR TURNBULL

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OIL PRICES

It looks as if BNOC's suppliers will be receiving around $1.25 per barrel less for their North Sea oil in June than they realised in May. Six months ago, that would have caused deep foreboding in the oil industry and sent shock waves through the foreign exchange markets. Recent soundings indicate that the oil companies are nervous, but not profoundly so. The sterling/dollar exchange rate fluttered on oil price fears, but has not gone into a nosedive.

Why the relative calm? The elimination of the BNOC clearing price as a touchstone of oil market pressures and sentiment, provides part, but not all, the answer. The underlying physical picture has not improved as far as OPEC's efforts to hold up oil prices are concerned. Medium-term world oil demand forecasts have, if anything, been shaded down over the last 6 months. Factors such as the foreseen turndown of the US economy and the conversion of some southern European power stations from oil to gas, have contributed. The anticipated peaking of non-OPEC oil production is now seen as slipping from 1985 to 1986. OPEC members will have to keep their belts tight for at least another year.

No-one, including OPEC, seriously expects the non-OPEC producers to curb their production, even if oil prices fall.

No-one foresees a further slide of oil prices restoring the growth of oil demand.

It is all on OPEC who, in spite of cheating by some members and sacrifices by others, doggedly maintain the balance of supply and demand. As before, there are good reasons why OPEC members could fall out in squabbling self-interest, leaving the oil price to spiral down. But the greatest self-interest lies in sticking together and patching up differences. That is likely to happen again and the markets anticipate it.

That may sound comforting, but the FSBR oil revenue forecast of £13.5 billion for 1985/6 looks like falling by upwards of £1.5 billion; the sterling price of oil is now subject to the twin pressures of weak dollar oil prices and stronger sterling.

JW

JOHN WYBREW