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E(79)68

22 November 1979 COPY NO 56

CABINET

MINISTERIAL COMMITTEE ON ECONOMIC STRATEGY

THE PRIVATISATION OF BNOC

Note by the Central Policy Review Staff

Introduction

1. In his paper on The Future of BNOC (E(79)67), the Secretary of State for Energy makes proposals of outstanding importance. There are very large amounts of money at stake in North Sea oil and, money apart, the security of oil supplies is crucial for us as for all industrial countries. The arguments and facts set out in E(79)67 are complex as well as important. We in the CPRS believe that more analysis is desirable before Ministers take the decisions set out in E(79)67, paragraph 20 "Conclusions and Recommendations".

Questions

2. As we in the CPRS see it, the main questions which deserve more analysis are -

(i) the potential cost to the PSBR of moving BNOC (Operating) into the private sector;

(ii) how to get the best price for the nation for whatever assets of BNOC (Operating) it is decided to sell;

(iii) the ability of BNOC (Trading) to maintain security of supplies against the pressure of the EEC Commission.

The PSBR

3. In PSBR terms, the privatisation of BNOC is different from British Airways and British Aerospace. BNOC, like British Gas, expects to make large annual positive contributions to the PSBR. The moment BNOC is privatised that positive contribution [say £400m. a year 1981/1985] is

lost and the difference will need to be made up each year by some combination of less public expenditure, higher taxes, or further asset sales. Privatising BNOC and selling £1 bn. of BNOC assets benefits the PSBR in the years in which those assets are sold, but the £1 bn. gained is purchased at a high price in terms of PSBR benefits stretching out into the future.

4. There are, of course, powerful political arguments for privatisation but compared with British Airways and British Aerospace the potential PSBR costs are such that they need very careful consideration. If what matters is money rather than the principle of privatisation, £1 bn. benefit could be obtained from the sale of assets while still keeping the positive cash flow benefiting the PSBR: e.g. there are various methods of selling £1 bn. of BNOC assets in non-voting form which would keep BNOC in the public sector and keep the positive cash flow of BNOC benefiting the PSBR.

Getting the best price for BNOC assets

5. There are two worries on selling BNOC assets for the best price: (i) oil assets are almost certain to rise in price in the years ahead; and (ii) BNOC shares have, as yet, no 'track record'.

6. These are not negligible points. The market does not always value adequately. Some 30 months ago HMG sold a tranche of BP shares (a world class stock with a good 'track record'). In those 30 months the FT Index has fallen markedly. But the price of BP shares has risen some 70 per cent (despite BP's knocks in Iran and Nigeria). If HMG had sold that first tranche at today's prices we would have received some £400m. more than we actually got for it.

7. If 'privatisation' as soon as possible is the objective then 51 per cent of BNOC shares need to be sold quickly. But in terms of getting the best price for the nation there is a case for spreading out the sales over a longer period.

8. Spreading out the sale does not necessarily mean putting off the gain to the PSBR. Earlier this year Ministers were reluctant to sell BNOC's assets in individual North Sea fields. To fill the gap in 1980/81 they asked BNOC to raise £500m. from forward sales. BNOC have been cautious and expect to raise £600m. If a better price for BNOC assets is likely to be obtained by spreading out sales, receipts could be brought forward (if that were desired) by some forward selling arrangement.

The security of supply and pressure from the EEC Commission

9. BNOC (Trading) is envisaged as a free standing public sector company whose main objective is not to make money (it would do well to break even) but to help secure oil supplies for the United Kingdom. (BNOC's own crude accounts for about half the 'secure' oil from the North Sea.) Some of the arrangements which we have made in the past are likely to be attacked by the EEC which is currently questioning a number of facets of our Continental Shelf regime and has successfully attacked one of them.

10. Would the creation of a separate BNOC (Trading), whose main object was security of supply, make us more liable to effective challenge by the EEC? A considered legal view on this is desirable.

Conclusion

11. In the light of the above questions (and Ministers may well have others) the CPRS would recommend that Ministers do not come to immediate decisions on the conclusions and recommendations set out in E(79)67, paragraph 20.

Cabinet Office
22 November 1979