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Prime Minister ✓



Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

These points can
be taken up
at the meeting
which we
have fixed
for Friday.

PRIME MINISTER

GOVERNMENT TO GOVERNMENT DEALS WITH OPEC

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17/12

David Howell sent me a copy of his minute to you of 12th December reporting on the outcome of the IEA Ministerial meeting on 10th December. In the penultimate paragraph of his minute he asked colleagues to agree by correspondence that he should pursue the question of Government to Government deals with the OPEC countries on the lines recommended in paragraph 5(a) of his paper on "Implications of Changes in the World Oil Market" (circulated under his Private Secretary's letter of 5th December).

2. Paragraph 5(a) of David Howell's paper invited colleagues to endorse:

"That officials should urgently evaluate the scope for, and relative merits of, establishing direct purchasing arrangements with OPEC Governments through BNOC, specially created subsidiaries of BP or Shell or major UK industrial oil consumers."

I certainly welcome the study proposed in paragraph 5(a), but I should want the opportunity to consider its results before there were any contacts with OPEC countries about Government to Government deals. I say this particularly because of the financial risks such deals may involve. Paragraph 38 of the report by officials attached to David Howell's paper rightly points out that the most

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important problem involved in the deals indicated in his paragraph 5(a) is the risk of financial loss to the Government. In the case of BNOC any loss incurred in the purchase of oil from OPEC countries would necessarily fall on public expenditure and the PSBR. Major industrial oil consumers which did not normally buy oil direct might well ask us to guarantee them against any losses incurred through purchases of OPEC oil undertaken with our encouragement. And as paragraph 38 pointed out, even in the case of specially created BP and Shell subsidiaries, the possibility of a request for Government underwriting cannot be ruled out. I can certainly see the potential advantages of the sort of deal referred to in paragraph 5(a), but I could not welcome any arrangement which exposed the Government to significant risk of loss with consequences for the PSBR. I hope therefore that officials in their further consideration can devise some arrangement which minimises the risk of financial loss to the public sector.

3. I see that officials commented in paragraph 37 of their report that in view of some OPEC Governments' wish to deal with State oil companies, BNOC looked to be the obvious choice for such deals though the Corporation's lack of refining interests might be a disqualification in the eyes of OPEC. If this is right, I wonder whether it has any bearing on our consideration of the future of BNOC? Would OPEC be even less willing to deal with BNOC if the Corporation was solely an oil trader without any oil fields of its own? I would be interested to have David Howell's views on this point. In any event we want to avoid the situation where BNOC is obtaining oil e.g. from Kuwait, at the expense of Shell and BP. The result then could be that our national oil supplies would not have increased but that business would have been transferred from the private sector to the public sector, perhaps at higher prices to OPEC. We clearly need to guard against this.

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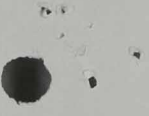
4. It is clear that while the objective of Government to Government deals is welcome, they do carry certain risks. As I have already said, I entirely agree that officials should further consider the possibility of such deals and indeed should, as they recommended in paragraph 9 of their report, discuss them with BNOC, BP and Shell and with ICI and other major oil purchasers, including the CEGB. I hope all this can be done so that we can come to some view before David Howell goes to the Middle East early in January. If it cannot, I think that he will have to be very guarded in any approach he makes to OPEC governments on the subject.

5. I am sending copies of this minute to Peter Carrington, David Howell, John Nott, Sir Robert Armstrong and Sir Kenneth Berrill.

A handwritten signature in black ink, appearing to be 'G.H.' with a stylized flourish.

(G.H.)

17 December, 1979



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