

PRIME MINISTER

THE GULF WAR AND THE INTERNATIONAL OIL MARKET

1 The war between Iran and Iraq has stopped exports of oil from both countries. Although the oil supply situation is manageable there are worrying signs that we may be in for another big increase in oil prices. How to handle this serious situation will be discussed at the Energy Council of the European Community on 27 November, at the European Council on 1/2 December and at the IEA Ministerial on 9 December. This minute seeks your agreement to the way in which I propose to approach these talks. I will put my final proposals to OD shortly before the IEA Ministerial.

2 The issues are examined in the attached paper by my officials. Treasury and FCO officials have been consulted, but it is not an agreed document.

3 We face a difficult choice and a problem of political saleability. There is no scarcity of oil. The problem is to prevent another massive price increase. It will not be easy to persuade UK consumers to accept for this purpose even minor restraints on their use of oil when North Sea production is in total sufficient to cover our needs. If anything more than very minor levels of restraint were called for this could only be secured by persuading or instructing the oil companies to reduce supplies, involving rough and ready justice between consumers. As the paper points out, there are doubts about how effective international action would prove to be in practice. And there are also doubts about whether it would be honestly and consistently applied by all our partners (I have the French particularly in mind).

4 Against this the UK, with its open economy, is especially vulnerable to the damaging effect of oil price rises on the world economy. The further loss of production in the short run which would result from another substantial price rise would limit even further our economic policy options and defer the time when our policies will start to produce results. The impact on United Kingdom

industry already under severe pressure would be serious. The disruptive internal impact, as the economy shifts still faster out of energy intensive industry, would be considerable. There is a limit to the speed with which the economy can cope with this process and we are close to that limit. The political consequences of all this need to be weighed against the political difficulties of persuading consumers to accept a limited reduction in their supplies of oil.

5 There is no question of our agreeing to international action unless all major industrial countries agree to take part and there are effective monitoring arrangements to ensure that that agreement is observed. It may be that the US will be unable to agree to substantive decisions on 9 December or that the French will be hamstrung by their forthcoming election. In that case only cosmetic decisions will be possible. But if our partners are prepared to agree on action - which is unlikely to involve drastic restraint of demand - the UK in my view cannot afford to stand out against the general wish; indeed it would be contrary to our wider interests to do so. It follows that we should handle the preliminary discussions in such a way ~~that~~ responsibility for any failure to agree will rest with those concerned and not the UK.

6 I therefore propose that our line in the preliminary official discussions and (subject to developments) at the Energy Council on 27 November should be:-

- (a) to let it be understood that we are willing to participate in international action only provided that it is unanimously supported by our partners and that satisfactory and effective monitoring arrangements are set up;
- (b) to let others take the lead in making specific proposals, but to give non-committal support to ideas which look sensible and which are consistent with UK interests;
- (c) to ensure that any arrangements proposed are satisfactory to the UK and that they give us a reasonable advantage as

an oil producer; we should be able to get our partners to understand and accept the political need for the latter points;

- (d) to keep open our position on the form which any action might take until what is proposed is clear; but if the prospect of a concerted international effort emerges, to try and edge things towards Option (iv) in the enclosed paper (a reduction in stocks and modest restraint of demand).

7 I should be glad to know if you and our colleagues concerned are content that we should proceed in this way.

8 I am sending copies of this minute and enclosures to the members of OD and Sir Robert Armstrong.

JA  
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Secretary of State for Energy  
17 November 1980

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