

MR TURNBULL

Prime Minister ②

To note that the process of winding
down BNOC is very largely
complete

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THE RUN-DOWN OF BNOC

Against the background of the current OPEC meeting, it occurs to me that you might like a note on the progress which has been made in running down BNOC, in case the Prime Minister should have any queries.

The 500,000 barrels per day (bpd) of oil available to BNOC under Participation Agreements has all been returned to the producers. Separate third-party contracts at the official BNOC price accounted for an additional 120,000 bpd. That volume has now been reduced to some 50,000 bpd, and within 2 months the Department of Energy expect it to be down to 20,000 bpd. Further pressure will be applied to the producers - which incidentally are likely to include Burmah - to withdraw voluntarily from the contracts.

In principle, it would be nice to wind up all these contracts and, with them, the existence of a BNOC official price. On the other hand, the BNOC official price is no longer a significant factor in the oil market. There is no merit in the Government attracting criticism by applying unreasonable pressure to the residue of small producers.

In any case, initial fears that the small producers would be taken to the cleaners by the large producers, who are the

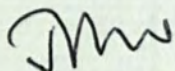
natural outlet for small additional streams of oil, have not materialised. Now that BNOC has withdrawn, some of the medium-sized producers are lifting their own oil and competing with the majors to offer attractive terms to mop up the small residual volumes from the minor producers.

The Government Oil Pipelines Agency is likely to be established either on 1 October or 1 December 1985, depending on whether the associated legislation is completed before or after the Summer Recess. The Department of Energy have had some difficulty in retaining a core of traders from BNOC. Assuming that GOPA continues to dispose of the Government's Royalty Oil (currently 250,000 bpd) a total manpower establishment of 40-45 is envisaged.

Some of the major oil companies with refineries in the UK - notably at this stage BP - are pressing the case to buy back the Royalty Oil relating to their own production. The attraction for them would be to run this oil through their own refineries. Because of difficulties in establishing an arm's length tax reference price, the rest of their production is normally traded through the spot market and, where necessary, bought back by the producers' subsidiaries. The Department of Energy have yet to reach a policy decision on whether or not to concede this. They feel that if the concession is made for one integrated oil company, they would have to make the concession for all. This would remove the majority of GOPA's availability from its

portfolio. The remaining trading operation would hardly be meaningful.

The removal of BNOC from the oil market is seen with hindsight as having eliminated two destabilising effects: the tendency for traders to speculate against BNOC whenever the oil market is critically weak; and the removal of a seller in the inherently weak position of having to sell a large volume of oil in a buyer's market. For all that, the oil market is still fragile.



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