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Prime Minister

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PRIME MINISTER

GULF VISIT: MAY 1983

As Secretary of State for Energy, I visited Kuwait, Saudi Arabia and Abu Dhabi between 1 and 5 May. This trip was planned originally for last September but was postponed twice for the convenience of my opposite numbers and then held up by the difficulties over Palestinian representation on the Arab League delegation's visit to London. These delays were fortuitous as, in the event, the visit took place immediately after the recent turmoil in the oil market and enabled me to build on the series of informal bilateral contacts which took place during that period.

2. The state of the oil market was inevitably the major topic of discussion. The other main issues to emerge were the oil slick, the Gulf countries' plans to develop and export their gas, and the prospects for nuclear power generation in the region. I also used any opportunities which arose to press our defence procurement interests.

The Oil Market

3. Appreciation of the UK's contribution, earlier this year, in helping to restore stability to the world oil market was reflected in the cordiality with which I was received. I found a wide consensus that the worst was over, that OPEC's London agreement was holding up unexpectedly well and that, although the market remained fragile, the $29 marker was likely to hold - perhaps even to the end of 1985.

We can expect the OPEC production quota to rise from 17.5 mbpd this year to 19 mbpd next, which will ease the revenue problems of a number of its members, particularly Nigeria and Venezuela. Indeed, there may be pressure for such an increase from the fourth quarter of 1983. All three countries I visited are clear that this would be undesirable and the Kuwaitis at least are prepared to contemplate a price increase of 50c a barrel if necessary to avoid it. The Saudis seemed reasonably content with their role as 'swing' producers while Dr Otaiba of the UAE confirmed that so far OPEC's Monitoring Committee had not found any cheating in relation to the London Agreement.

4. By common consent, the Nigerians are seen as the weakest link in the OPEC chain (and the Libyans as the least predictable). It is because North Sea oil competes directly with Nigerian that OPEC regards our position as so important. Accordingly, I was closely questioned about our production plans for this year and next. I explained that although crude oil production had been running at nearly 2.3 mbpd in the first quarter of 1983, over the year as a whole it was likely to be broadly similar to last year's level of 2.1 mbpd. There would be a slight increase in 1984 and 1985, after which the level of production in the North Sea would begin to decline.

5. However, the Kuwaitis went further in that Shaikh Ali Khalifa argued (as agreed in advance, I suspect, with Yamani) for more formal relations between OPEC and non-OPEC producers in the interests of 'stability'. I am in no doubt that the intention behind this proposal was to press us into production controls to parallel OPEC's. I therefore made it clear that we thought informal bilateral contacts were most productive and that we could not contemplate any production controls in the period ahead.

Community Oil Tax

6. Yamani had heard that the European Community was considering an import tax on oil and he went out of his way to underline his opposition to the idea which he said (somewhat improbably) was certain to provoke OPEC into imposing a matching export tax. I explained that excise duties on oil had been examined in the context of the Community's search for new sources of revenue but that they had not found favour. Yamani expressed relief, adding that it was important to allow falling oil prices to stimulate demand. This is, of course, an essential part of OPEC's current strategy for survival.

Gulf Refinery Capacity

7. I took the opportunity of my visit to explore the Gulf States' intentions over the build up of local refinery capacity. (As you know, there is surplus capacity worldwide at present and the oil companies have been closing plant in the UK and elsewhere in Europe). The Assistant Secretary General of OAPEC, Abdul Aziz al Wattari, admitted that there was pressure for ever increasing local refinery capacity but said that he did not see it coming to pass. In his view, local demand for oil products was growing faster than anywhere else in the world and, on current plans, there would be no net product exports from the Gulf by 1990. However, the Saudis expect to be exporting 2 mbpd of products by that date and the Kuwaitis already have ½ mbpd of export capacity which they hope to increase slightly by meeting their internal demand from gas instead of oil.

8. The Kuwaiti national oil company, KPC, is continuing its aggressive pursuit of overseas acquisitions. It hopes to increase its oil production from the North Sea (and elsewhere) and remains keen on distributing oil products in the UK. Negotiations for the purchase of the Gulf oil company's UK downstream interests, including their share in the joint Texaco/Gulf 'cracker' at Milford Haven are continuing but KPC are concerned that they might have to close Gulf's

associated refinery a year or two after acquisition. I told Ali Khalifa that we would not welcome such a closure.

The Oil Slick

9. There was great uncertainty about all aspects of this problem. Estimates of the leakage varied from 2,000 to 7,000 barrels a day and information on the size, location and movement of the slick was sparse and contradictory. Little or no oil had come ashore and there need not be major problems provided that the leakage could be stopped fairly soon. The Iraqis are being blamed for having prevented this so far.

10. The general expectation seemed to be that most of the oil would either evaporate or come ashore on the largely uninhabited Iranian coastline. Although concern on the Arabian shore increased as one moves south, I did not get the impression of any real urgency about anti-pollution measures. Indeed, despite the message you received through Ian Lloyd on 30 April, the President of the Saudi Ports Authority failed to take the opportunity of meeting me. Nevertheless, I advertised the UK's abilities and willingness to help as widely as possible. More recent press reports suggest that more oil is hitting the Saudi coast than the few tar balls which I was shown in Dhahran.

Gas

11. In my view, confirmed by Otaiba when I put it to him, most of the Gulf States are in no hurry to develop their gas reserves for export - the Kuwaitis have stopped exploration for gas, the Saudis are maintaining only a token effort, and countries like the UAE and Qatar, with large reserves already proven, are reluctant to see it sold to their neighbours. The Quataris, whose oil reserves are closest to exhaustion are likely to be the first to export gas but even they have missed the boat to some extent by seeking terms which

the oil companies find much too onerous in today's market. The other countries, whose oil reserves will last for very many years to come, think of their gas as a potential competitor with their oil at present but a source of revenue once the oil begins to run out. Otaiba told me with some pride that Abu Dhabi had secured the world's highest prices for its existing gas exports, adding that if everyone in the Gulf had been as tough, the oil market would be stronger than it is today. Ali Khalifa questioned me closely on the extent to which we saw a need for new sources of gas to meet European requirements.

Nuclear Power

12. Ali Khalifa is exploring the idea of building a low temperature reactor in Kuwait to help acclimatise the region to the idea of civil nuclear power. He thinks that a low temperature reactor would be more acceptable politically than, say, a PWR but is concerned that no-one (ie the Israelis) should be able to say that Kuwait is acquiring stocks of nuclear fuel for other purposes. Nor does he wish to be reliant on a single source, in this case France, for the technology and so would like to combine Swedish expertise with our fuel cycle capabilities and Kuwaiti engineering as a counterweight. He has already discussed these ideas with the AEA and I encouraged him to talk further as well as to BNFL and my Department.

13. Abu Dhabi also has nuclear power in mind for electricity supply and desalination and Otaiba said that a decision in principle to proceed might be taken by 1985. He would like to send a technical delegation to the UK. He also suggested that Qatar and the Saudi Eastern Province might be interested in the project.

Conclusion

14. The trip, though brief, was a useful development of the informal contacts with my opposite numbers that served us well

during the oil market difficulties in the first quarter of the year. The Gulf States attribute to us an important role in stabilising oil prices and therefore have a clear interest in good and close bilateral relations on oil matters at least for the time being.

15. When I called on the Amir of Kuwait, I expressed disappointment that he would be unable to pay a State Visit to Britain this year. He replied that he would very much like to consider a visit in future when circumstances in the Gulf were less difficult. He also asked me to pass on to you his warm personal regards.

16. I am copying this minute to my successor as Secretary of State for Energy, and to the Secretaries of State for Foreign and Commonwealth Affairs, Defence, Industry and Trade, and to Sir Robert Armstrong.

NL

(Nigel Lawson)
13 June 1983