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OIL DIVISION
DEPARTMENT OF ENERGY

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Benjamin
16 January 1986
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CONFIDENTIAL

P Henley Esq
Export Credit Guarantee Department
Aldermanbury House
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Dear Henley,

I have seen a copy of Bob Adam's letter to you of 13 January, in which he suggests that we should advise you on the appropriate assumptions to make about the oil market and the Saudi economy.

As far as the Saudi economy is concerned, I would have thought you should discuss this with the Bank, FCO's economic advisers (Guy Gantley) and the Cabinet Office. I have to say that I share many of the misgivings in Downing's letter of 9 January.

As for the oil market, there is, as you know, considerable downward pressure on crude oil prices at present. Most estimates of the call on OPEC crude in Q1 1986 put it at some 2 to 3 million barrels/day below current OPEC production of some 18 mbpd; and Saudi Arabia has publicly given up its role as swing producer. Moreover, demand for oil takes some time to respond to changes in price. In the short term, a return to production restraint by OPEC members, including Saudi Arabia, is likely to be the only effective way of stabilising prices; but this is unlikely to happen, if it happens at all, until prices have fallen some way from present levels. I think you could therefore make a good case for analysing your proposal on a lower base case assumption of \$20 pb. But I think it would be best if you discussed with the Treasury the energy price assumptions they are making, so that there is no difference between you on this point. I would only add the oil market is at present dominated by the uncertainties over OPEC's future; and you will probably wish to reflect these in any conclusions you reach.

Although I appreciate your wish to conclude arrangements soon, there could be some advantage in delay. There is to be a meeting early in February of the Ministerial Committee set up by the last OPEC conference to make recommendations on how to defend OPEC's market share; the market is likely to react to this meeting; and we may then have a better idea of future developments.

Yours sincerely
William Rickett

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